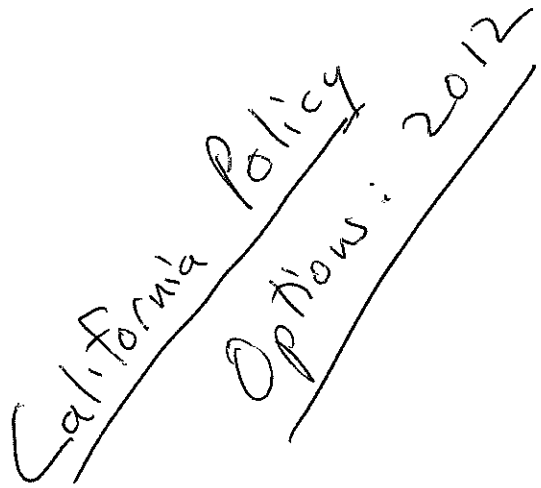
REALLY! NO MENTAL RESERVATIONS:

JERRY BROWN INHERITS CALIFORNIA'S BUDGET CRISIS



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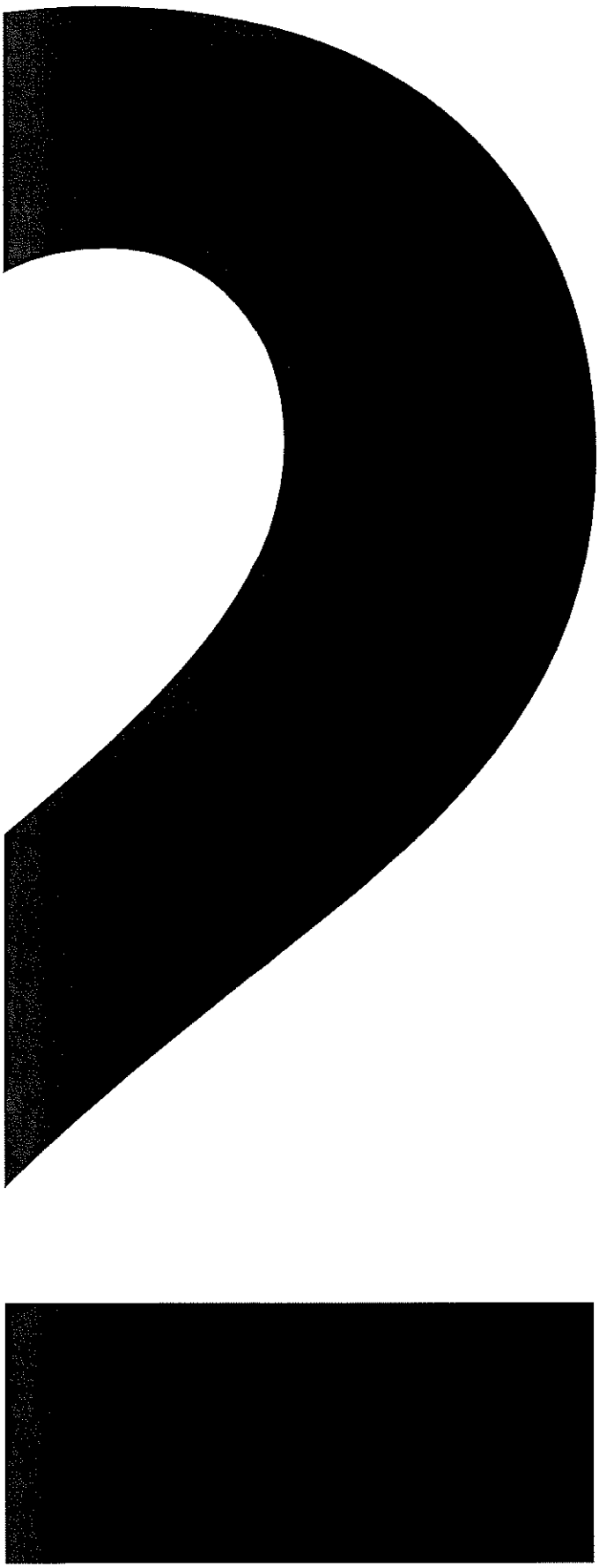


Justice Tani Gorre Cantil-Sakauye (administering oath of office): ...that I take this obligation freely...

Governor-Elect Jerry Brown...that I take this obligation freely...

Cantil-Sakauye: ...without any mental reservations.

Brown: ...without any mental reservations.

(Laughter from audience)

Brown: ...Really! No mental reservations!

The April 23, 2011 edition of the *Economist* magazine devoted a large section to California under the title "Where it All Went Wrong."[1] Its answer to the question was the state's direct democracy (initiative, referendum, and recall) system. Initiatives in particular were the villain, producing ballot-box budgeting formulas that hamstrung the legislature. Especially after the passage of Prop 13 in 1978—the initiative that dramatically cut property taxes and imposed a two-thirds vote for tax increases—so the narrative went, direct democracy in California had gone mad.

At around the time the edition appeared, the *Economist* co-sponsored a public forum at UCLA on the subject of California's dysfunctional government in which the thesis of runaway direct democracy was again put forth. While other panelists went along with the thesis, this author thought the matter was more complicated. It is certainly possible to show the contribution of direct democracy to California's fiscal problems. However, the gridlock and inability to pass a budget in an orderly fashion also characterize the U.S. Congress, although there is no direct democracy and no Prop 13 at the national level.

If there is communality of dysfunction at the U.S. and California state levels, it is party polarization and a need for a supermajority vote on critical issues.

Polarization is not a function of direct democracy. At the U.S. level, the supermajority hurdle exists due to Senate rules, not because of something imposed directly by the voters. At the state level, supermajority hurdles *are* related to direct democracy. But—as it turned later—direct democracy in California had (partially) made a self-correction. Voters ended the two-thirds vote requirement to pass a state budget in November 2010. As it turned out, that change allowed a new state budget to be enacted—after an initial failure—before the fiscal year 2010-11 expired.

In this chapter, we examine both the underlying problems in budgeting in California and the events that produced the 2011-12 budget. In earlier editions of *California Policy Options*, I have traced California budget woes over the years. And indeed, there is no single starting point for those woes since each budget year sets the preconditions for the next. However, in *California Policy Options 2011*, we took the budget tale up through the (much-delayed) passage of the 2010-11 budget, stopping shortly before the gubernatorial election of 2010. After some background on the budget process and its history, I will pick up the story from that point, stopping this time shortly after the 2011-12 budget was enacted and signed.

UNDERLYING CAUSE OR INSTITUTIONAL ARRANGEMENTS?

"...What is unique about California is not its set of challenges...which differ in scale but not in kind from those elsewhere. It is its brand of democracy..."

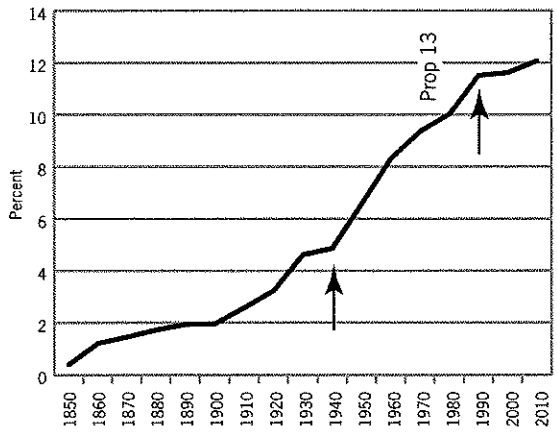
—Economist magazine[2]

It is easy to point to direct democracy—as the *Economist* did—as a factor in California dysfunction. At a fundamental level, since there is an alternative route to lawmaking without going through the legislature, the legislature is inherently weakened—since it can be bypassed and checked. Most of what a governor wants to accomplish requires legislative agreement and action—governors have more often than not been unsuccessful in using initiatives to bypass the legislature. So a weak legislature produces a weak governor.

However, particularly with regard to budgeting, what is occurring in legislating is allocating resources. Allocating resources is easier when the economic pie is growing rapidly. Rapid growth translates into rising tax receipts. In that context, allocating more money to program A does not require reducing program B by that amount or raising tax rates.

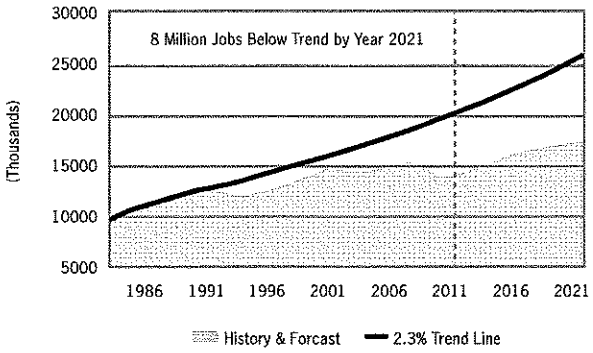
Figure 1 shows California's population as a proportion of the U.S. population. Generally, California has grown faster than the U.S. since statehood by that measure. But there are two obvious inflection points. After 1940, California's rising share of the U.S. population accelerates. After 1990, it decelerates. The period after 1940 marks the jump in federal military expenditures in California connected with World War II, the Korean and Vietnam Wars, and the Cold War. The year 1990 marks the end of the Cold War.

Figure 1: California Population Relative to US



Source: U.S. Bureau of the Census.

Figure 2: California Nonfarm Employment History & Forecast Vs. 2.3% Trend from 1990:3



Source: UCLA Anderson Forecast, June 2012.

Figure 2—a regular feature from the UCLA Anderson quarterly economic forecast publication—shows the old rapid trend of employment growth and California's departure from that trend after 1990. Even the dot-com boom of the late 1990s and the housing/mortgage boom of the mid-2000s do not close the gap between the old trend line and the actual outcome. In a sense, California has never recovered from the recession of the early 1990s, but no one has told the electorate. Perhaps California political leaders also need to be informed that the rapidly-growing pie they used to have for allocation no longer exists. In any event, fiscal institutions that worked tolerably well in the context of rapid expansion came under strain when Harder Times arrived.

A LOOK AT THE NUMBERS

"That's the art of politics. You can't win everything."

—Governor Arnold Schwarzenegger commenting on the October 2010 budget deal[3]

Chapters on the state budget in prior editions of California have traced the ups and downs of the state budget during the 2000s. **Table 1** uses the cash statements of the state controller to provide a brief summary. The state's General Fund can be thought of as a checking account in which funds are flowing in from deposits and out from expenditures. At any point in time, there is a balance in the account but in the case of the General Fund, the balance can be negative, i.e., the account can be overdrawn. At points during the year, because of seasonal mismatches between when revenue is received, mainly from taxes, and when expenditures are made, there can be an overdrawn account. In such cases, the state Treasurer may borrow externally short term (within the fiscal year) by issuing Revenue Anticipation Notes (RANs). Or there may be internal borrowing from various special funds outside the general fund.

Table 1: General Fund Debt, Cash, and Disbursements ($ billions or percent)

Year Ending June 30	Short Term Debt*	Cash Balance	Total Cash**	Disbursements	Debt as Percent of Disbursements
1998	$0	$0.9	$1.0	$53.1	0.0%
1999	0	0.8	2.1	58.6	0.0
2000	0	8.5	9.3	64.5	0.0
2001	0	3.4	3.6	83.5	0.0
2002	10.4	0.0	0.0	80.4	12.9
2003	11.0	0.4	3.0	78.7	14.0
First issuance of Economic Recovery Bonds* **					
2004	0	0.5	2.8	79.6	0.0
2005	0	6.4	7.2	82.0	0.0
2006	0	9.2	10.5	91.5	0.0
2007	0	2.5	4.1	104.1	0.0
Second issuance of Economic Recovery Bonds** **					
2008	1.5	0.0	0.9	107.3	1.4
2009	11.9	0.0	0.0	98.2	12.1
2010	9.9	0.0	0.0	86.7	11.4
2011	8.2	0.0	0.0	93.8	8.7

*Outstanding loans.
**Differs from cash balance by Special Fund for Economic Uncertainties (a "rainy day" fund maintained for the General Fund).
***Refinanced short term debt on a longer-term basis.
****Issuance of remaining authorized Economic Recovery Bonds allowing longer-term funding of short term debt.

Source: June cash reports of the State Controller.

When the account is overdrawn because of a longer-term problem than seasonality, there can also be internal borrowing. Essentially, an IOU is put into state other accounts. However, continually drawing from other accounts will eventually pinch whatever specialized service they provide. In relatively rare occasions, the state—through the state controller—can float Revenue Anticipation Warrants (RAWs) which provide borrowing from one fiscal year to the next. The interest rates the state has to pay on RANs and RAWs will vary with the risk of default that financial markets perceive. Ratings agencies—Fitch, Moody's, and Standard and Poor's—provide rating of risk on California financial securities.

The state constitution prohibits long-term borrowing for the kind of ongoing operating expenses which the General Fund encompasses. Such borrowing is essentially reserved for long-term projects such as infrastructure. The underlying concept is that projects that will provide service over a long period of time can (should) be paid for by users over that period. Even then, a vote of the people is required before General Obligation (GO) bonds—backed by the full faith and credit of the state—are issued. However, voters can also amend the state constitution to provide an exception, as occurred in 2004 after Governor Arnold Schwarzenegger took office in a 2003 recall election that replaced incumbent Governor Gray Davis.

Davis had come up with a plan to refinance state short-term debt through long-term borrowing which was intended to circumvent the constitutional limitations on borrowing and the requirement of approval by the electorate. It is doubtful that—given the legal cloud hanging over the Davis plan—it could have been successful. However, incoming Governor Schwarzenegger capitalized on his initial popularity and persuaded the electorate to approve the issuance of Economic Recovery Bonds under Props 57 and 58 of spring 2004. Most of these bonds were issued shortly after the election. But some remained authorized but not issued. Governor Schwarzenegger issued the remaining bonds in 2008 as part of the recurring budget crisis. Thus, there are three distinct periods of debt: Before the first Schwarzenegger bonds (through the 2002-03 fiscal year), after the first Schwarzenegger bonds until the second issuance (through the 2006-07 fiscal year), and the period since.

Table 1 traces the history of state debt in the General Fund from the late 1990s (during the dot-com boom) through fiscal year 2010-11 that ended June 30, 2011 with the three periods shown separately. The state built up a considerable cash reserve by 1999-2000 but at what should have been the peak of the cycle, began to pull down its cash (run a budget deficit). Running a deficit at the peak can only bring major problem at the trough which is what happened. Thus, although the ongoing budget problem was stabilizing at the time of the 2003 recall, the state faced the problem of dealing with a large short-term debt that needed to be rolled over at potentially high interest rates.

Once the special Schwarzenegger bonds were issued, thus refinancing the debt, and as the economy continued to recover from the 2001 recession/dot-com bust, the cash balance in the general fund rose. But much of the recovery in California was based on the housing/mortgage bubble which began to burst after 2006, and which shows up on Table 1 as a draw-down of cash during 2006-07. The housing/mortgage bust turned into a global financial crisis in 2008, leading to a state cash crisis and a build-up of general fund debt that peaked in 2008-09 and was reflected in the state's inability to pay all bills in summer 2009 and its issuance of IOUs (known as "registered warrants"). However, as will be discussed further below, the budget situation stabilized thereafter, thanks to a combination of budget cuts and temporary tax increases enacted by the legislature in February 2009.

FEBRUARY 2009, MAY 2009, AND THE LEGACY FOR THE NEXT GOVERNOR

"The current governor and prior governors have tried to bring people (in the legislature) together with little success."

—Neil Hokanson of Hokanson Associates wealth management[4]

Voters were offered the option of extending the temporary tax increases (income tax, sales tax, and vehicle license fee) in a special election in May 2009 but declined to endorse the extensions. The budget situation stabilized thanks to a variety of one-time fixes and cuts in 2009-10 and 2010-11. But that left a considerable debt in the General Fund to be financed—shades of the problem facing Governor Davis at the time of the 2003 recall. Unlike that situation, however, the Great Recession was followed by a very sluggish recovery and the specter of the expiring temporary taxes in 2011. Hence, whoever was elected governor in 2010 would have to deal with a budget crisis that was part financing and part the threat of new deficits.

Table 2 shows the credit ratings of California General Obligation bonds by the three major credit rating agencies. Ratings were generally upgraded after the first Schwarzenegger bonds were issued and the budget picture and the state economy generally improved. In 2009, however, the budget situation deteriorated again and California's rating fell to the lowest of any state. Since that time, no substantive changes were perceived by the rating agencies although two of them "recalibrated" all of their municipal bond grades, in part due to complaints of excessive negativity in ratings of the public versus the private sectors.

Table 2: California General Obligation Bonds Credit Ratings

	Fitch	Moody's	Standard & Poor's
Prior Rating	A (July '05)	A2 (May '05)	A (Aug '04)
May 2006		A1	A+
June 2006	A+		
Feb. 2009			A
Mar. 2009	A	A2	
July 2009	BBB	Baa1	
Jan. 2010			A-***
Apr. 2010	A-**	A1**	

*Prior rating is the rating that existed before 2006. Date in parentheses is the date that rating was first determined.
**Fitch and Moody's "recalibrated" their municipal bond ratings at this time and indicated the change in their ratings did not reflect an improvement in quality.
***After the 2011-12 budget was passed, S&P classified it's A- rating as "stable" on July 7, 2011.

Note: The three agencies use different letter grades. For Fitch, in descending order of quality: AAA, AA, A, BBB, BB, B (with plus and minus grades as shown). For Moody's: Aaa, Aa, A, Baa, Ba, B, Caa, Ca, C (with numerical add-ons as shown). For Standard & Poor's: AAA, AA, A, BBB, BBB-, BB+, BB, CCC, CC, C, D (with plus and minus grades as shown).

Source: California Treasurer website: http://www.treasurer.ca.gov/ratings/history.asp

THE LEAD-UP TO THE 2010 GUBERNATORIAL ELECTION

"Polls schmolls. The only poll that really matters is the poll on Election Day."[5]

—Gubernatorial candidate Meg Whitman a few days before November 2010 election

Although the gubernatorial election was not exclusively about the budget, the ongoing budget crisis remained in the background as a symptom of government dysfunction. The fact that a budget for 2010-11, which was supposed to begin on July 1, was not adopted until

October reinforced the sense of gridlock in Sacramento. Easy and grossly misinformed comparisons were often made between the near-bankrupt country of Greece and California, although bond rating agencies did not endorse the supposed analogy.[6]

There never was much of a gubernatorial contest in the Democratic side. For a time, Gavin Newsom, then-mayor of San Francisco, tried to run but never seemed to make a dent in the frontrunner, attorney general and former governor Jerry Brown. Brown didn't seem to have to do anything to be the frontrunner. Newsom eventually switched to the Lieutenant Governor race (and won the nomination and the general election). There was talk about Los Angeles mayor Antonio Villaraigosa running for governor. But he never did, in part because his municipal budget problems did not create confidence that he could meet the state's fiscal challenge.

The Republican contest was decidedly more heated. Former eBay chief executive, Meg Whitman—with seemingly unlimited self-funding—made herself the frontrunner in the primary, running against state insurance commissioner Steve Poizner, another former Silicon Valley executive. For a time, Tom Campbell, former UC-Berkeley and Stanford academic, former congressman, and former budget director under Governor Schwarzenegger, was also in the race. But unlike Whitman and Poizner, he had little funding and eventually switched to the U.S. senate race (and lost in a three-way contest in the Republican primary).

Whitman positioned herself as a non-politician outsider and promised business-type solutions—and no new taxes—to the state budge. That was an approach that had worked for Arnold Schwarzenegger in the 2003 recall when he defeated career politician and incumbent Governor Gray Davis. Indeed, Whitman went further than just a no-new-tax pledge and favored eliminating the capital gains tax. But by summer 2010, Schwarzenegger's poll ratings had fallen to roughly those of Davis at the time of the recall. So emulating Schwarzenegger's 2003 approach—even while distancing herself from Schwarzenegger, the man—was problematic.

One of Brown's more effective TV ads reminded voters of the similarity in approach of Whitman and Schwarzenegger. The ad was later dubbed the best negative ad in the country by a *Washington Post* columnist.[7] Conservative Republicans—particularly upset that Schwarzenegger had okayed a tax-raising deal in February 2009 with the legislature—depicted a Whitman victory as just a *de facto* third term for Schwarzenegger. On the influential Los Angeles area "John and Ken" talk radio show, Whitman received an unfriendly grilling while Brown was treated surprisingly gently.

Meanwhile, there was an undertow of bad personal publicity about Whitman. Whitman had had some kind of altercation with another executive at eBay and had to pay damages. Negative stories about obnoxious behavior by her sons circulated on the Internet on sites such as Gawker. Questions about excessive executive pay she received were raised. But what seemed to do the most damage was the so-called housekeeper-gate affair.

Whitman had fired her housekeeper in a reportedly nasty fashion when it came to light the housekeeper was an illegal immigrant. Prominent attorney Gloria Allred brought legal action related to the firing and the tearful housekeeper appeared on a TV news conference.[8] Up to that point, polls had suggested Whitman and Brown were tied in the race. After the affair broke, Brown moved ahead, particularly after Whitman—who was forced into a tough, but not always consistent, anti-illegal immigration stance in the primary—said on Fox News that her housekeeper should be deported. As former GOP state senate leader Jim Brulte said after Whitman's election loss, "I don't know how you can be a billionaire, say someone is

part of your family, fire her, and not even give her enough severance... or at least (not) hire a lawyer to help her."[9]

Brown pointed to his past experience as governor (1979-83) in a selective manner, emphasizing his experience in dealing with the political institutions of the state. He did not point to the major budget crisis he left to his successor, George Deukmejian, although older voters apparently remembered and tilted toward Whitman.[10] On taxes, he promised there would be no new ones *without a vote of the people* (an important proviso).

Rather than provide specific budget solutions, however, Brown emphasized process. He would work out a bipartisan budget deal with the legislature using knowledge that only a longtime California politician could have. Whereas Whitman explicitly pushed for moving away from defined-benefit pension plans for public employees—noting the underfunded status of such plans in California—Brown simply said he would work on some kind of pension reform.

While Whitman was left to deal with housekeeper-gate shortly before the election, Brown didn't have any diversions of that magnitude. The closest he came was "whore-gate," an episode in which he had left a voicemail message for an unfriendly union official and did not hang up, thus leaving a recording of a subsequent political conversation among his advisors on the machine. Someone—not Brown—called Whitman a "whore" in that conversation for favoring retaining defined-benefit pensions for police in contrast with other public workers. The suggestion was that she had done so to obtain endorsements from police unions.[11] But since it was never clear who said it, and since the reference in fact did emphasize Whitman's contradictory exemption of police from her pension policy, whore-gate quickly faded while housekeeper-gate stuck.

Ultimately, opposing Brown and promoting the whore-gate affair was seen as a blunder by the union involved and its chief political consultant. "I'm like Casey at the Bat; I stuck out," said the union's advisor.[12] But most other unions had backed Brown and felt they had an "in" with the governor.

That position was less clear for the business community, which generally had supported Whitman. In particular, the California Chamber of Commerce had run an ill-disguised attack ad on Brown on TV in the spring of 2010, leading to an outcry and a quick pulling of the ad. "That's in the past," the Chamber's president said, hopefully, in December 2010 after the election, although it was not clear that all was immediately forgotten or forgiven.[13] However, the Chamber had favored the unsuccessful tax extension measure in May 2009. It similarly gave general support to the idea when Brown as governor tried for a second extension measure in 2011. Brown termed the Chamber's position in 2011 as "forthright and positive."[14]

In the end, Whitman—after a campaign expenditure estimated at $177 million—lost badly to Brown (who spent $36 million), pulling in fewer votes than an initiative—Prop 19—legalizing marijuana, which also lost.[15] Eighty-one percent of Whitman's spending was self-financed. (Election results are summarized on **Table 3**.) Despite a national shift toward Republicans, California voters produced a Democratic sweep of all statewide offices and re-elected U.S. Senator Barbara Boxer to another term.[16] Whitman largely disappeared from public view for several months after the November 2010 election. But she was quoted in mid-April 2011 as suggesting that she had come to believe that the "immigration discussion" was "not helpful" for Republicans.[17]

Table 3: November 2010 Election Results (percent of votes in favor)

Prop 19:	Legalize marijuana	46.5%
Prop 20:	Independent commission to redistrict congressional seats*	61.3
Prop 21:	$18 tax on vehicles for state parks	42.7
Prop 22:	Prohibit state from taking (borrowing) various local agency funds including transit agencies	60.7
Prop 23:	Suspend AB32 (greenhouse gas law)	38.4
Prop 24:	Repeal business tax breaks enacted as part of Feb. 2009 budget deal	41.9
Prop 25:	Simple majority vote (instead of 2/3) to pass state budget	55.1
Prop 26:	2/3 vote for fee increases & retaining fuel tax swap of 2010-11	52.5
Prop 27:	Kill independent redistricting Commission*	40.5
	Jerry Brown for governor	53.9
	Meg Whitman for governor	40.9

*An earlier proposition passed in 2008 created an independent redistricting commission charged with redistricting the legislature, not state congressional districts, after the 2010 Census became available. Prop 20 added congressional districts. Prop 27 would have terminated the commission and returned redistricting to the legislature.

Source: California Secretary of State, *Statement of Vote, November 2, 2010 General Election*, revised January 6, 2011, http://www.sos.ca.gov/elections/sov/2010-general/complete-sov.pdf

Although legalizing marijuana lost (in spite of claims that legalized marijuana could be a tax source for the state), voters approved other budget-related measures. They tightened up the tax vs. fee distinction, making it more difficult to raise revenue via the latter, under Prop 26. Covered fee increases would now require the same two-thirds vote that tax increases already required. In contrast, an initiative (Prop 21) that would have imposed a car tax to support state parks (and provided free entrance to parks by California cars) was defeated.

An attempt to repeal certain business tax breaks (Prop 24) that were part of the February 2009 budget deal also failed with voters. Another proposition (Prop 22) made it more difficult to dip into revenues of local entities such as transit districts and redevelopment agencies. As it turned out for the latter agencies, Prop 22 morphed a few months later into a case of be-careful-what-you-wish-for, an outcome to be discussed below.

Republicans interpreted these actions of the electorate in November 2010 as a continuing voter anti-tax mood. On the other hand, voters changed the two-thirds requirement to pass a budget—a requirement that went back to the Great Depression—to a simple majority under Prop 25. In effect, the Democratic majority could pass a budget without Republican support, *so long as no tax increases were included* (a major limitation). A failure to pass a budget by the constitutional deadline of June 15 would result in forfeiture of legislators' pay (not just a delay in pay) for each day beyond the deadline. The combination of Brown's political pledge that any tax increases would require a vote of the people, the remaining two-thirds vote hurdles on taxes and fees, and Prop 25 were to become the major ingredients in the eventual tax deal of June 2011.

TAX BACKGROUND

"...We just have to get those tax extensions because the alternative is not pretty."

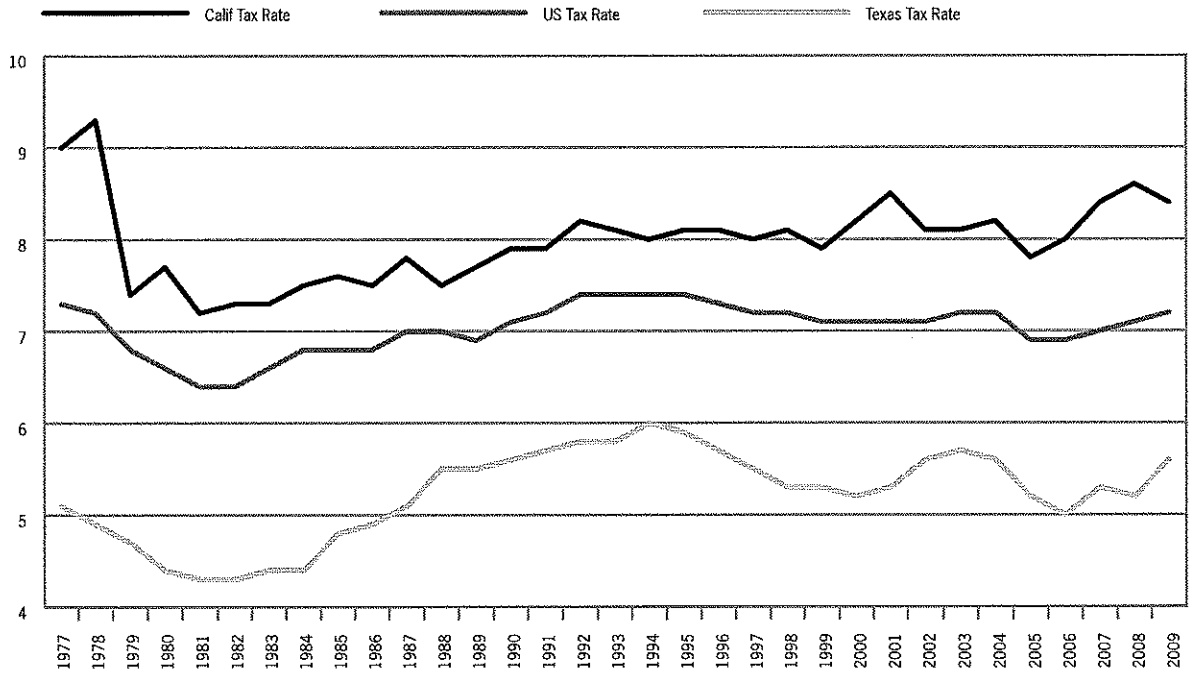
—Governor Jerry Brown soon after a self-imposed deadline for putting tax extensions on the ballot had come and gone[18]

"If somebody was designing a tax system from scratch, it's a good bet it wouldn't look like what we have today. Practically nothing in California politics is by design."

—Professor Jack Pitney, Claremont-McKenna College[19]

Much controversy surrounds California taxes and their comparison with those of other states. During the 2011 budget discussions, Texas was often brought in for comparison on the grounds that its taxes were attracting jobs. California was depicted—especially by Republicans—as a high tax state that was losing jobs as a result.

Figure 3: Own State & Local Tax Rate Per Dollar of Personal Income (percent)



Note: US tax rate refers to average state and local taxes across all states and does not include federal taxes.

Source: Chart based on Tax Foundation data. See text and notes for details.

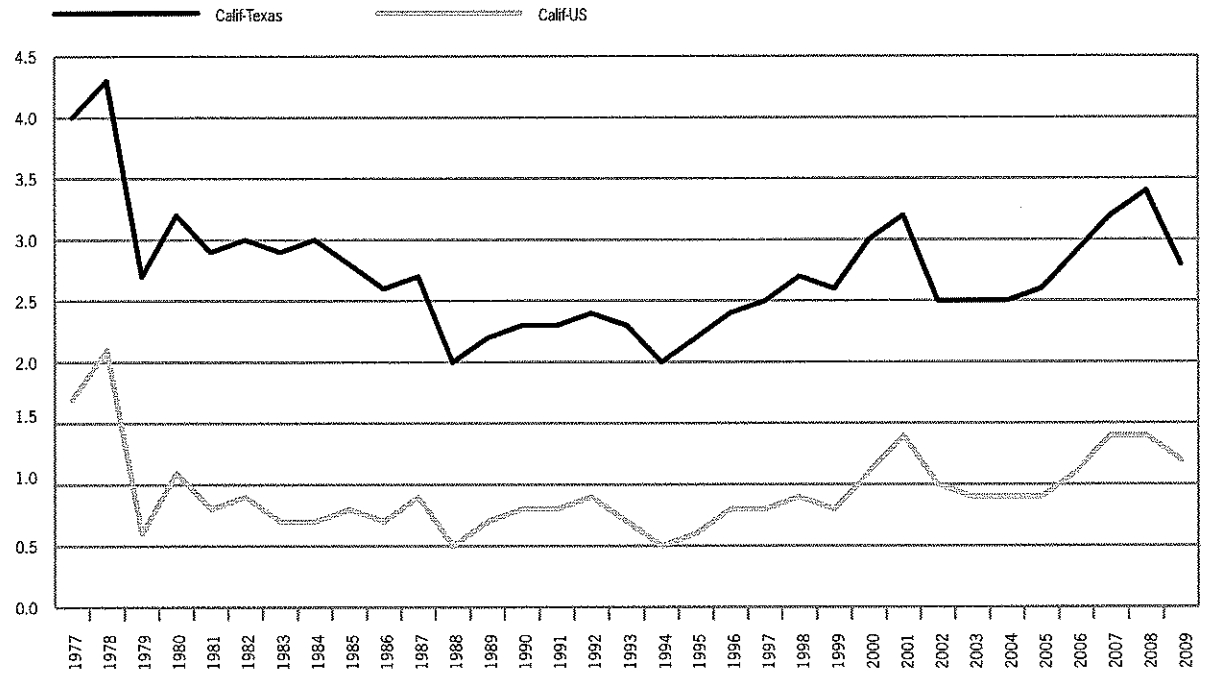
Figure 3 shows that, indeed, California state and local taxes as a percent of personal income are somewhat higher than the national average and notably higher than those of Texas.[20] (Comparisons across states must be made on a state-*and-local* basis since the division of responsibility for funding and providing particular services such as education varies across states.) On the other hand, as **Figure 4** illustrates, the gap between Texas and California state and local taxes by that same measure has not changed much over time.

Finally, **Figure 5** indicates that California state and local taxes on a per capita basis run about 30% above the national average while Texas state and local are about 30% below that average. Texas is definitely a low-tax/low-public-service state. California has higher taxes but its appetite for services tends to exceed its revenue base.

It should be stressed that these measures are all based on averages, not on marginal tax rates. Economic theory suggests that decisions by individuals or firms about where to locate are likely to be based on importantly on marginal rates. In addition, there is an intangible factor of tax stability. If the tax code is constantly in flux—which can happen if there are chronic budget crises—it becomes difficult for businesses to plan.

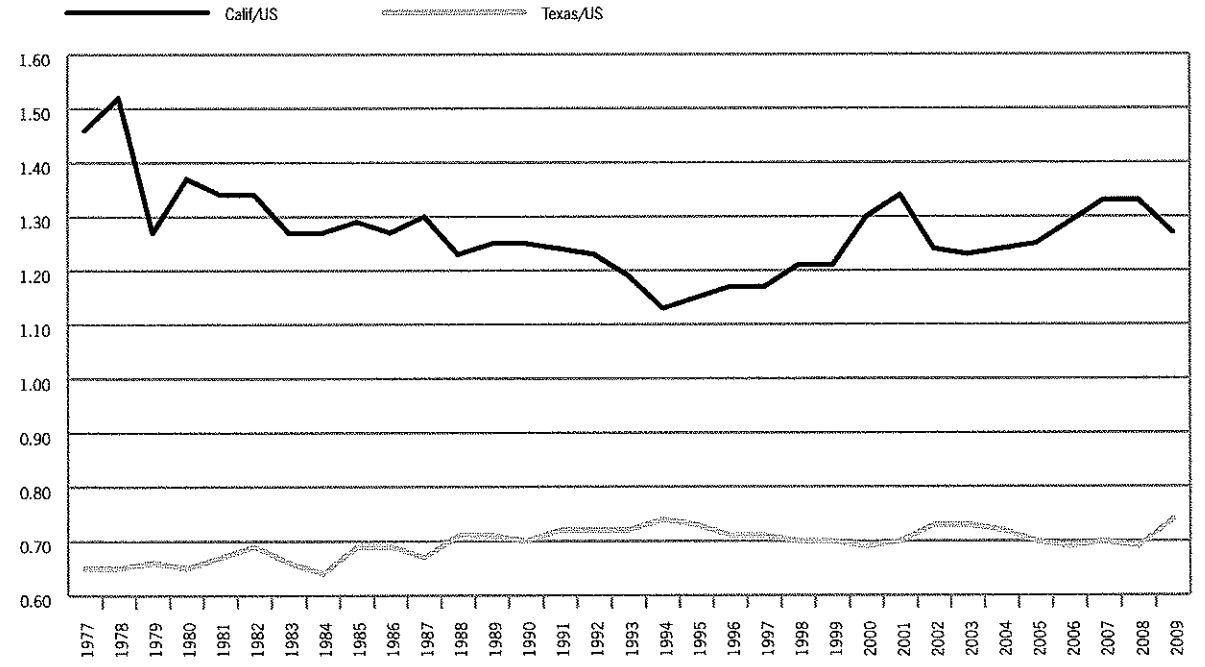
Two features stand out from these charts concerning California taxes. First, the big drop in taxes after Prop 13 was passed in 1978 is apparent. There is some erratic upward creep in California taxes over the period shown but not back to the pre-Prop 13 levels. Second, the impact of California's heavy reliance on the progressive income tax (in part because of its lesser reliance on

Figure 4: Own State and Local Tax Rate Gap: California vs. Texas and California vs. US (percentage points)



Source: Chart based on Tax Foundation data. See text and notes for details.

Figure 5: Own State & Local Taxes in Per Capita Dollars vs. US Per Capita Average (ratio)



Source: Chart based on Tax Foundation data. See text and notes for details.

property taxes after Prop 13) shows up in the variability and timing of the ups and downs of California taxes. California is heavily dependent on the fortunes (and misfortunes) of higher-income taxpayers. The dot-com/stock boom of the late 1990s is clearly visible in the form of an upward jump in the California measures. The housing boom of the early-to-mid 2000s is similarly visible. In contrast, Texas has no income tax so when there is a burst of personal income in that state, its revenues as a percent of personal income tend to fall.

As noted earlier, there was a major turning point for California when the Cold War ended and employment fell. The drop off in federal military spending in the state corresponds to the longer term slowdown in the state's growth relative to the rest of the U.S. The California-Texas tax gap was present when California was growing rapidly during the Cold War but also present afterwards. For that matter, the taxpayer revolt surround Prop 13 was not based on popular concern about employment trends—that is a more contemporary argument. The issue at the time of Prop 13 was the tax burden itself and a sense that rising property taxes were not producing a corresponding jump in the quality of state and local services.

HOW NOW, BROWN GOVERNOR?

"It's very fortunate when I had no primary opposition... And then, of course, you have my sparkling personality."[21]

—Governor-elect Jerry Brown explaining his victory the day after Election Day

"(The budget situation) is certainly as bad as anyone—as it's ever been."[22]

—Governor-elect Brown after meeting with Department of Finance officials

By constitutional mandate, governors must deliver a state-of-the-state message and produce a budget proposal in early January. For incoming governors, the challenge is especially daunting since new staff must be hired and brought up to speed between Election Day and January. Brown began his preparation by meeting with Department of Finance staff and soon reappointing Governor Schwarzenegger's finance director Ana Matosantos. He undertook symbolic steps such as rejecting the usual provision of rented office space normally given to governors-elect for the transition. That move was a throwback to his previous governorship in which he rejected living in what was then a newly-built governor's mansion.

But while the transition was going on, other budget-related events were occurring. The University of California (UC) Regents raised tuition despite student protests and UC recruitment of out-of-state students (who pay higher tuition than residents) continued. Litigation—mainly unsuccessfully—challenging state employee furloughs invoked by Governor Schwarzenegger continued. Court decisions and/or litigation challenging this or that budget cut proceeded. Various state unions agreed to concession deals, reducing state payroll costs. Governor Schwarzenegger, despite his lame duck status, called

a special session of the legislature to deal with the budget. The Schwarzenegger administration also pursued its (extremely dubious) plan to sell state office buildings and lease them back (a kind of high-cost loan).[23]

Meanwhile, weak market demand for California state securities led to a cancellation of a planned bond offering. And voter attitudes remained contradictory. In the abstract, voters say they favor spending cuts rather than tax increases when polled. But when asked what to cut, the only category toward which voters tilt is prisons—presumably because voters' concept of prison spending is coddling criminals. Yet federal courts have been pushing the state to spend *more*, not less, on prisons—which account for about a tenth of the general fund—and/or to release prisoners if more is not spent.

One problem is that issues that state politicos think are important are not the major preoccupation of the electorate, although, of course, voters express themselves by voting on who and what appear on the ballot. In a poll undertaken shortly after the November 2010 election, voters were asked what they thought was the most important issue facing the state. Sixty-four percent said it was "jobs, economy" while only 13% said it was "state budget, deficit, taxes."[24] These poll results are consistent with others taken in the aftermath of the Great Recession. It is often said, for example, that voters in California are very concerned about education. But the same poll indicated that 4% thought "education, schools" was the most important issue.

To try and focus public attention on the budget, Governor-elect Brown, State Treasurer Bill Lockyer, and State Superintendent-elect of Public Instruction Tom Torlakson went on a road show complete with PowerPoint charts and graphs on fiscal matters. How much public attention was paid to the details on the charts and graphs, however, is open to question. A public opinion poll in January showed that the usual contradictions and confusions over the budget remained untouched. When asked what they would like to cut, seventy percent said "prisons and corrections." No other category received even close to a majority.[25]

Meanwhile, outgoing Governor Schwarzenegger's special legislative session on the budget opened in early December. It is noteworthy, however, that his proposals to the legislature were mainly cuts. They did not include extending the expiring temporary taxes that became the centerpiece of Governor Brown's initial budget proposals after he took office.

As a lame duck with only a few weeks in office to go, and with low popularity rating, Governor Schwarzenegger's proposals were not really considered seriously. A former Schwarzenegger finance director conceded in an op-ed defending the governor's budgetary record that the structural fiscal problems the governor had inherited had not been resolved.[26] As his term came to an end, Governor Schwarzenegger dealt with budget-related political debts, appointing two GOP assemblymen to state commissions; both had paid heavy political prices for going along with the governor in February 2009 on temporary tax increases.[27]

But he also reduced the prison sentence of the son of former Assembly Speak Fabian Núñez who had been convicted of murder, creating a mini-scandal.[28] In an interview shortly after leaving office, Schwarzenegger indicated that his wife and children broke into tears when his gubernatorial work schedule kept him in Sacramento and away from his family.[29] But a still larger scandal developed later when it came out that Schwarzenegger had fathered a child by a domestic servant in his household, unbeknownst to his wife who subsequently started divorce proceedings.

In seven years, Schwarzenegger—elected in the 2003 recall largely due to the budget crisis of that era—had

gone from Terminator to Governator to Inseminator in the public mind. At the end of his term, the departing governor posted a Twitter video of him walking out of his office and turning off the light and essentially disappeared from the California political scene. State Treasurer Bill Lockyer, a Democrat who—at the time of the recall indicated he had voted for Schwarzenegger—said that in retrospect "I guess I should have just abstained entirely, said nothing, (except) just stick with Gray (Davis)."[30] His musing seemed to be a more general public sentiment. But that sense of public regret would not solve the budget problems facing the governor-elect.

MOVING TOWARD SPECIFICS

"I'd say he thinks like more of a visionary and I'm more 'let's make sure every train is running on time...'"

—Anne Gust, wife of Governor-elect Jerry Brown explaining her role as unpaid gubernatorial advisor[31]

"The next step is serious public conversation with the people of California about what they want from their government, what they expect and what they are willing to pay for."

—Governor-elect Jerry Brown[32]

Whatever the changes in politics and public opinion were in the aftermath of the November election, the specifics of a budget proposal had to be formulated quickly. There were the usual uncertainties about the direction of the economy and other contingencies. For example, the issue of state prison overcrowding was argued before the U.S. Supreme Court soon after the election. The Court's eventual decision would have a fiscal impact but no one could know for sure what that decision or impact would be. As governor, Jerry Brown characterized the Court's eventual decision as a "sword of Damocles" hanging over the state budget.[33]

An appeal by the state on revenues from Indian gambling was also before the Supreme Court. And there was still some residual litigation over state worker furloughs that had been imposed for budget reasons by the Schwarzenegger administration. Generally, the state had been successful in past litigation in defending these furloughs but some questions remained, particularly in the case of employees in agencies who were not paid from the General Fund. Furloughs functioned as a bargaining chip the state had with its unions in negotiating other contract concessions under Governor Schwarzenegger.[34] Generally, his furloughs ended in calendar 2011 but were replaced by "personal leave days" which had much the same effect.

The November election at the national level gave Republicans control of the House of Representatives, making state receipt of more federal stimulus-type funding highly unlikely. In early January, the Federal Reserve indicated it would not loan directly to state and local governments, in part because of legal restrictions on such actions. And a federal deal between the Obama administration and Congressional Republicans on the estate tax indirectly worsened California's budget picture.

On the other hand, a California Board of Equalization report pointed to a potential new source of revenue. Californians technically were supposed to pay sales tax on Internet purchases from out-of-state retailers such as Amazon but rarely (almost never) took it upon themselves to pay the tax to the state.[35] An explicit obligation of such retailers to collect the tax would bring in over $1 billion, according to the report.[36] Ultimately, that observation led to enactment of an "Amazon tax" as part of the 2011-12 budget.[37]

As the date in which he would take office approached, Governor-elect Brown indicated that explicit borrowing was not something he wanted to do, i.e., he seemed to want to avoid a multi-year workout solution

of the type Governors Schwarzenegger and Pete Wilson had undertaken.[38] And Brown indicated that he wanted a budget deal wrapped up in 60 days after he made his formal budget proposal. Moreover, he began to spell out more general plans to put extensions of the temporary taxes that would otherwise expire in 2011 on the ballot and to shift various programs to local governments, the term of art for the latter being "realignment." One attraction of such realignment is that removing spending from the General Fund tends to reduce K-14 spending mandated by Prop 98 (1988).

Inauguration day brought a speech by the new governor that had elements of old Jerry Brown as well as new. Brown indicated he had read prior governors' inaugural addresses—a "sobering and enlightening" experience and noted that they all start on a high note and then go into the problems of the day. He determined "that what we face together as Californians are not so much problems but rather conditions, life's inherent difficulties."

The element of old Jerry Brown was the suggestion that the budget was an ongoing "condition" and the abstract idea that "problem(s) can be solved but a condition always remains." But the new Jerry Brown was also present in promises of "an honest budget" that would be a "tough budget for tough times" and the statement that he would not "embrace delay or denial." Whereas old Jerry Brown was known for contemplation and a lack of budget focus, the new one would focus on the nitty-gritty of budget negotiations. And, as it turned out, for the first six months of his term, the governor was almost entirely focused on the budget.[39]

Between the inaugural and the presentation of the budget, there were mainly signals from the governor. On the one hand, Brown showed up at a public union event, but did not speak to the audience and left quickly. The message seemed to be that he would not be beholden to the unions that had supported him in the election. On the other hand, he appointed a labor lawyer who had represented the prison guards' union to be his personnel director, signaling that he hoped for a cooperative approach in negotiating various labor agreements that needed to be concluded.

Behind the scenes, a budget strategy had to be determined. The decision to ask voters whether to extend the temporary taxes that were expiring in 2011 had already been made. But it was known that voters had rejected such an extension in May 2009. They might well reject extensions again. Brown could have come in with an all-cuts "budget from Hell" to show what would occur if there was a rejection. He could then have posed an alternative, less-severe budget with the added revenue from tax extensions.

Perhaps the budget from Hell would have persuaded voters to look favorably on extensions as a way out of Hell. The danger, however, was that a budget from Hell might be attacked by liberal Democrats on whom Brown was counting. There might not even be a majority vote to be had for such a budget if liberals were offended. In addition, state treasurer Bill Lockyer argued that there could be a backlash if Brown "seem(ed) to be threatening voters."[40]

Another approach was to present a budget proposal which *assumed* that there would be a vote on tax extensions and that voters would approve them. It could then simply be said that since such a budget would still involve significant cuts, voters could presume that an undisclosed budget from Hell would be much worse—but without details. The choice was made to go with a budget that assumed a vote which approved extensions.

There was a third alternative, one the Legislative Analyst pointed to, in which some kind of multi-year workout budget would be presented with temporary measures and implicit borrowing. Although that approach could be derided as "kicking the can down

the road" or "smoke and mirrors," it had merits that deserved attention given the alternatives. But the multi-year workout approach was not considered, seemingly ruled out by Brown's pledge of an "honest budget" and his expressed disdain for borrowing.

THE JANUARY BUDGET

"For ten years, we've had budget gimmicks and tricks that pushed us deep into debt. We must now return California to fiscal responsibility..."

—Governor Jerry Brown presenting his January budget proposal[41]

"There are not votes in the Assembly Republican Caucus to place the same tax increases that voters overwhelmingly rejected less than two years ago back on the ballot."

—Assembly Republican leader Connie Conway[42]

"Voters were given this choice (extending temporary taxes) back in 2009 and they rejected it and frankly they were right to reject it."

—Senate Republican leader Bob Dutton[43]

The governor's January budget was, as had been expected, a mix of extensions of the temporary tax increases that had been approved in February 2009 but which would require a vote of the electorate and spending cuts. He wanted a special election on the extensions sometime in June.44 One way of putting the extensions on the ballot would have been via initiative, i.e., signature gathering. But Brown chose instead to do it via the legislature which would seemingly require a two-thirds vote and, therefore, some Republican support; four legislative Republicans would be needed. The notion was that if there was some Republican support, even just the minimum four, the ballot propositions could be depicted as bipartisan, which—it was believed—would enhance the chance for approval. Brown knew that voters had rejected extensions in May 2009 so the bipartisan label would be desirable to induce a change of mind.

If the initiative process had been started immediately, there might have been enough time to put the choice before voters by June. But starting that process and also asking for the alternative—legislative approval—would have undermined any chance of Republican support. Why would Republican legislators, given the high price of cooperating with the governor, want to vote for something that would be on the ballot anyway if they didn't cooperate? Conceivably, with the governor desiring to go only via the bipartisan legislative route, Republicans could negotiate with him about the budget itself and anything else they might want. As the minority party, they might achieve some goals otherwise beyond their reach.

However, as the quotes at the outset of this section suggest, Republicans declared immediately that they would not cooperate with the tax extensions. Brown evidently did not take them at their word and seemed to view such statements as negotiating ploys. His assessment turned out to be a mistake; they were true to their word in the end.

Brown asked for approval of the extension ballot proposition and the budget as a whole in 60 days, ostensibly to provide enough time for the mechanics of a special election to function. (In fact, there was more time and the actual deadline from an administrative viewpoint was fuzzy and flexible.) But once the clock had run on the 60 days, there was no way that a petition process for an alternative initiative could accomplish his objective by June. Brown also declared a new fiscal emergency which superseded the emergency declared by Governor Schwarzenegger in December.

From the Republican perspective, running the clock was a desirable strategy. Under Prop 25 that voters

had recently approved, a cuts-only budget could be approved by a simple majority. So Republican votes were not needed if that painful route were eventually chosen. Democrats would be blamed for the cuts in that event, since they had the needed simple majority. Republican Senator Bob Huff signaled that Republicans would not need to come up with a cuts—only budget themselves. "It's a majority-vote budget," he said. We're not the majority. We respect that. We'll be part of the process but it's not like we're going to lead with all the things where we become the bad guys."[45]

Indeed, Republicans set out to prove that there might be a way for Democrats in the legislature to put tax extensions on the ballot as modifications of prior initiatives. They were able to obtain a limited legal opinion, seeming to endorse that view. According to a Republican spokesperson, the opinion suggested that Democrats were just looking for "political cover" in asking for GOP votes.[46]

But in fact, following a legally-questionable approach would probably have failed. A court might well have enjoined the process and pushed whatever election there was—if it were ultimately allowed—well beyond June. However, the objective from the Republican perspective was mainly to indicate that Brown and the Democrats didn't need Republican support and should go ahead on their own (and answer to the electorate for what followed). Assembly speaker John Pérez complained that Republicans were "trying to abdicate their responsibility" by raising the simple-majority approach.[47]

Even had the governor ultimately received sufficient support from Republicans to put his tax extensions on the ballot, a court opinion in late January suggested that the wording of the ballot title and summary would not be in the control of the legislature. Initiatives that are filed receive a title and summary from the Attorney General and that language can have an influence on voter receptiveness. However, the legislature had in earlier propositions that it had placed on the ballot reserved the right to create its own (enticing) language for the title and summary. In a case involving legislature-determined language for a 2008 bond proposition for high-speed rail, it was ruled that the legislature could not author the language but, as in the case of initiatives, would have to rely on the Attorney General.[48]

As will be described below, in the end Brown did not receive Republican support and there was no special election. Such an election—had it occurred—would not have been confined to Brown's tax extensions and would have included any initiative that had previously qualified plus a constitutional amendment passed by the legislature in October 2010 involving an enhanced "rainy day" fund.[49] A budget was passed eventually that did not include extensions and thus had more severe cuts than if extension revenues had been part of the package.

Given hindsight, and given the statements made by Republicans initially, it can be asked why Brown continued for almost six months to try and negotiate a deal with them. Democratic leaders in the legislature came to the conclusion more quickly than Brown that no deal could be reached but could not proceed until he signaled that negotiations had failed. It may have been that Brown's approach was reflective of his earlier terms as governor in which the legislature was less polarized and in which bipartisan deal-making was commonplace.

As for the numbers, **Table 4** summarizes the Legislative Analyst's budget estimates as of November 2010. **Table 5** summarizes the governor's January 2011 proposals. Brown's revenue estimates with no tax extensions were more pessimistic than the Legislative Analyst had made in November. Thus, absent any modifications, the 2010-11 budge—instead of showing a slight surplus—was about $2 billion in deficit. Some of the discrepancy between the Legislative Analyst's numbers and the governor's involve a change in accounting accrual practices,

apparently made to reduce the Prop 98 guarantees to K-14 education.[50]

Table 4: The Budget as Seen by the LAO in November 2010 ($ millions)

	FY 2009-2010	FY 2010-2011	FY 2011-2012*
Fund Balance Start of Year	-$5,375	-$5,371	-4,591
Revenue & Transfers	87,041	93,284	83,530
Expenditures	87,037	92,505	102,756
Surplus/Deficit	+4	+797	-19,226
Fund Balance End of Year	-5,371	-4,591	-23,817

*Workload estimate.

Source: Legislative Analyst's Office, *The 2011-12 Budget: California's Fiscal Outlook*, November 2010, p. 3

Table 5: The January 2011 Budget Proposal ($ millions)

	LAO: Nov 2010 2010-2011*	Governor: No Change 2010-2011	Governor: Proposal 2010-2011
Fund Balance Start of Year	-$5,371	-$5,342	-$5,342
Revenue & Transfers	$93,284	$90,687	$94,194
Expenditures	$92,505	$92,793	$92,209
Surplus/Deficit	+$797	-$2,106	+$1,985
Fund Balance End of Year	-$4,591	-$7,448	-$3,357

	2011-2012*	2011-2012	2011-2012
Fund Balance Start of Year	-$4,591	-$7,448	-$3,357
Revenue & Transfers	$83,530	$83,513	$89,696
Expenditures	$102,756	$100,749	$84,614
Surplus/Deficit	-$19,226	-$17,236	$5,082
Fund Balance End of Year	-$23,817	-$24,684	+$1,725

*Same as Table 4. Note: Accrual accounting practice changes were made in the January 2011 budget proposal that are not reflected in the LAO's November 2010 estimates.

Source: California Governor, *2011-12 Governor's Budget Summary*, January 2011.

Brown's proposal would have made a mid-year change in the ongoing 2010-11 budget, moving it into a $2 billion surplus, a swing of $4 billion. Extension of the income tax surcharge was part of that swing. On the other hand, Brown projected the no-policy-change/workload budget for 2011-12 to have somewhat lower expenditures than the LAO had assumed. In the end, however, both LAO and the governor indicated that the General Fund, if no changes were made, would have a negative balance on the order of $24 billion by June 30, 2012. Neither version was sustainable; there would have to be policy changes.

Brown's chosen method of presenting his proposals for the remainder of budget year 2010-11 and the upcoming 2011-12 year roughly characterized his approach as half tax extensions and half spending cuts. That division may have been framed to sound like an obvious compromise. However, the revenue jump in the combined two years was about $9.7 billion and some of that increase was natural growth from economic recovery, anemic though it may be. The combined expenditure cuts from the no-policy-change budgets of the two years were about $16.8 billion.[51] So the Brown proposals were in fact heavier on the cuts side than on the revenue side.

Moreover, if Brown were willing to accept simply a non-negative fund balance as of June 30, 2012 rather than the approximately $2 billion he targeted, he could do with somewhat less of a revenue increase than he proposed, maybe about $8 billion. If some good news on revenues came along and boosted the revenue estimate—something that ultimately happened—he could do with even less. If he did the proposed expenditure cuts first, i.e., if he could persuade the majority Democrats to approve them, the only thing that would be left on the table were revenues from tax extensions. And if a deal for those extensions fell through, a combination of optimistic revenue assumptions and incremental cuts above the January proposals would produce a budget that at least "balanced" by some definition on paper. Essentially, that is what occurred although it took six months and much *Sturm und Drang* to get there.

GETTING THERE: PART 1—EARLY NEGOTIATIONS AND CONTROVERSY

"Those of you who'd like to argue a little longer, or advocate, well, maybe come on over. I'll give you a cup of coffee."

—Governor Jerry Brown to a group of local officials upset about his plan to abolish redevelopment agencies[52]

"You can't build a budget on the assumption that you will lose in court. State government would come to a screeching halt."

—Department of Finance spokesperson H.D. Palmer[53]

There were controversial elements in the new budget. Although voters in November 2010 (Prop 24) had rejected repealing various tax breaks for business that had been included in the February 2009 budget deal, Brown proposed eliminating one of them which, it was argued, fostered moving jobs out of state. He proposed delaying issuance of previously-authorized bonds for transportation projects to avoid debt service on those bonds in 2011-12.

Of course, most of the complaints about the budget came as a result of cuts in allocations to particular programs ranging from higher education to courts and to social services including health care. From January onwards, there were protests about such cuts and lobbying aimed at persuading the legislature to reject them. In some cases, litigation was filed or threatened.

As part of his attempt to sell his budget/tax extension proposal, the governor undertook symbolic actions aimed at demonstrating frugality, i.e., taking away state worker cell phones and automobiles. In a move somewhat reminiscent of Governor Schwarzenegger's first term, he asked for a study on reducing waste in government and improving efficiency. In Schwarzenegger's case, an elaborate study produced volumes of analysis that ended up forgotten. Governor Brown's effort was less extensive. He asked the state auditor for suggestions and she sent a short list without attaching a tabulation of the actual savings that could be achieved.[54]

REDEVELOPMENT

The issue that raised the most heat was proposed abolition of local redevelopment agencies. Such agencies are set up by municipal governments to undertake what used to be called "urban renewal," a phrase that now has a negative connotation. Essentially, the agencies rely on "tax increment" financing for various development projects.[55] An agency will undertake, often in partnership with private developers, projects that—if successful—will raise property values. The increase in property values is earmarked for the agency to use for paying off bonds it issued to finance the redevelopment.[56]

As the state's budget problems worsened, it found various ways to raid local funding including those of redevelopment agencies. In response, as noted earlier, voters approved Prop 22 in November 2010 which made such raiding more difficult. Governor Brown might have done some raiding of redevelopment agencies had Prop 22 not passed. But since the new proposition precluded that approach, he proposed simply to abolish the agencies. If they did not exist, rechanneling their funds would not be a raid.

In the convoluted intertwining of state and local finance, particularly in the wake of Prop 98 of 1988 that guarantees funding to K-14 education, the diversion by redevelopment agencies of property taxes takes money

from schools which the state makes up. Ending that diversion reduces the state's obligation. In the governor's plan, there would be a one-time contribution from redevelopment agency abolition in 2011-12 of $1.7 billion. Past debt service of the agencies would continue to be paid until the obligations ended. And those revenues not needed for debt service after 2011-12 would go to the locals thereafter, in effect funding some of the realignment shift of state responsibilities to the locals.

Redevelopment agencies, however, are usually big operations and often have strong support from local political officials since they allow local enhancement of economic activity. There is much controversy about the net effect of redevelopment agencies, i.e., whether they are worth their cost or are doing Good Works. But local governments clearly were upset at the prospect of having them abolished. Indeed, Prop 22 was supposed to protect the agencies' funding, not kill them outright.

Examples of some of the redevelopment projects funded in Los Angeles, or slated to be funded, include a downtown streetcar, the fostering of a "Cleantech" manufacturing area, and a mixed-use plan for Grand Avenue in the area of the Disney Hall and Music Center. In addition, some municipalities had found ways of covering some city expenses. City workers who really handle basic municipal operations might be placed on agency payrolls.

Moreover, redevelopment agencies are local entities and result from local municipal decisions. The Brown budget in part was based on "realignment," which—as noted earlier—meant transferring responsibilities from the state to the locals. Even if redevelopment agencies make bad decisions (or if municipalities make mistakes in creating these agencies)—as critics argued—it seemed contradictory to tell locals that they would be given more responsibility while at the same time taking away their authority to promote redevelopment. In effect, the contradiction was to give locals more authority on one hand but tell them bad decisions were forbidden on the other. Making mistakes is inherent in having responsibility and even in the best of circumstances, there will be errors of judgment.

In any event, the proposal to abolish redevelopment agencies guaranteed legal challenges, particularly given Prop 22, the popularity of redevelopment among local political leaders, and the considerable influence the agencies themselves had accrued over the years.[57] It also set in motion a perverse rush by local governments and redevelopment agencies to approve projects—some undoubtedly hastily planned—to commit the agencies to the projects before they were abolished. The governor's initial proposal seemed to permit and grandfather project continuation and repayment of existing obligations.

As the rush continued—there were threats to amend the proposal to terminate recent projects. In addition, to circumvent Prop 22's ban on raiding the agencies' funds by the state, the governor's plan for the first year—when the agencies had not yet ceased to exist—created an intermediate entity to do the raiding and then pass the money to the state. The Legislative Counsel (not to be confused with the Legislative Analyst) opined that this indirect raid was not legal and the money could not be passed to the state. The Department of Finance declared that it disagreed with that interpretation. But the episode foreshadowed the eventual legal challenges to the redevelopment plan that followed passage of the 2011-12 budget.[58]

PUBLIC WORKERS AND PUBLIC PENSIONS

Around the country, Republican governors began varying degrees of attack on collective bargaining rights for state and local employees. Unions overwhelmingly give their political support—both

in dollars and in in-kind get-out-the-vote efforts—to Democrats. The Republican argument was that unions were negotiating overly-generous pay and benefits and that these costs were harmful to distressed public budgets. The State of Wisconsin was home to an especially bitter legislative battle over the collective bargaining issue.[59] There was also a brief push to have Congress (now that the House was under Republican control) create a legal mechanism for states to declare bankruptcy—presumably allowing state governments to void or renegotiate existing collective bargaining agreements. The idea was dropped when it seemed likely that allowing such bankruptcy would tend to undermine the market for state government bonds.[60]

In California, where unionization is higher than the national average, almost entirely because of higher unionization rates in the public sector, collective bargaining as a legislative issue did not arise because of Democratic control and the general tilt of state politics. However, in particular localities—notably the City of Costa Mesa—there was a Wisconsin-type battle. That small city managed to garner statewide attention when one employee committed suicide after receiving a layoff notice.[61] Palo Alto's city council voted to put on the ballot a proposition that would end that city's compulsory (binding) arbitration system for settling labor dispute impasses.

While collective bargaining *per se* was not a major issue in California, public pensions became a proxy for that issue, although many nonunion employees in the state are covered by pension systems. Pensions essentially come in two flavors: "traditional" defined benefit pensions and "401k"-type defined contribution pensions.[62] The former involve the creation of a pension fund which receives employer and employee contributions in varying proportions to pay benefits to retirees. Those benefits are based on a formula typically involving age, length of service, and earnings history of the beneficiaries. Defined contribution plans—in contrast—are essentially tax-favored savings accounts for individual workers which receive employer and employee contributions. Covered workers generally have a choice of investments such as stock funds, bond funds, and less risky assets such as certificates of deposit.

Under defined contribution plans, employees on retirement have a sum of money reflecting contributions and investment returns—whatever those turn out to be. The risks entailed due to investments that don't pan out or due to inadequate contributions over the years are borne by the employee. Under defined benefit plans, investment risks are covered by the employer since the eventual monthly pension is determined by formula. In the private sector, defined benefit plans were commonly components of union contracts but as unionization declined in private employment, so—too—did defined benefits there. In the public sector, defined benefit plans actually predated unions; when public sector unionization came along—mainly in the 1960s, 1970s, and 1980s—unions essentially inherited an employment system which came with such pensions.

Defined benefit plans can become underfunded since ultimately the plans must pay the accrued benefits whether or not sufficiently funding has been gathered from contributions and investment earnings. By definition, defined contribution plans cannot be underfunded since the employer owes only the contribution it puts in and those contributions are made upfront. If those contributions—or the investment income the employee derives from them—prove to be inadequate to support the employee in retirement in the style he/she might have expected, that is the misfortune of the employee/retiree, not of the public employer.

California has three major state pension funds. CalPERS covers most state employees, apart from those of the University of California, and the

employees of local governments—other than schools—that are part of the system. (Some local governments—such as the City of Los Angeles—run their own pension systems and are not part of CalPERS.) CalSTRS covers teachers in school districts around the state. Finally, the University of California runs its own pension system. (The California State University system—CSU—is part of CalPERS.)

All three of these state systems were significantly underfunded during the period when the budget for 2011-12 was under negotiation. A significant part of the unfunded liability was due to the stock market decline associated with the financial crisis of 2008 and the Great Recession. There was also a past history of underfunding and improvements in the pension formula from the employee perspective during the dot-com boom, improvements premised on unrealistic projections of fund earnings.

The University of California had a unique pension problem. Its plan had long been *over*funded thanks to good investment returns and had experienced—as a result—a two-decade period in which the plan received no contributions (employer or employee). Prior to this long contribution "holiday," the state had paid the employer contribution. Even before the 2008 financial collapse, it had long been known that the holiday would have to end once the funding ratio dipped below 100%. But when that happened, the state took the position that it had no responsibility for the UC pension system. The earlier history of state contributions was forgotten.

Largely due to outside revenues from hospital operations and research grants, roughly $2 out of $3 that would go into the UC pension fund if there were employer contributions would come from *non-state* sources. But if the state (or the Regents) did not pay into the fund for employees who were state-funded, the other non-state contributions could not be collected. Another way of posing this problem is that each $1 *not* put in by the state (or Regents) costs the pension fund an additional $2. During budget crises in the early 1980s and 1990s, the legislature—while strapped for immediate cash—made its contribution in the form of an IOU to the plan, payable over an extended period. This time, however, even the IOU solution was not implemented.

In earlier budget legislation for 2009-10, the legislature had actually declared that it had *no* responsibility for the UC pension system. It later was persuaded to delete that declaration. However, there was no money appropriated for the UC pension contribution despite the deletion. The Regents modified the pension plan for new hires in December 2010 and began a scheduled ramping up of employer and employee contributions. However, the failure of the state to make contributions to the UC pension, even in the form of an IOU, meant that the seeming equality of budget cuts to UC and CSU was in fact heavier on the UC side. CSU did not have to make pension contributions from whatever it received from the state. And, absent hospitals and major research grants, it did not have the $2-for-$1 problem. UC had to restart pension contributions and do so out of the general appropriation of the state for core educational functions.

During the 2010 gubernatorial election, Meg Whitman pushed for conversion of public pensions to defined contribution, both state and local. (She made an exception for police which, as noted above, was the central element in the "whore-gate" affair.) Jerry Brown talked about pension reform but was vaguer on the details. Part of the issue is that there is strong legal support for the position that public sector pension promises that have accrued cannot be reduced.[63]

It was clear that new hires could be put under a less-generous system, whether defined benefit or defined contribution. It was less clear whether changes could be made in the formulas covering current workers. If the formulas could be changed going

forward, in effect such workers would be guaranteed whatever they had accrued under the old system but would thereafter accrue at a lower rate under some new system, or be given a defined contribution plan. Even if that were legal, exactly how it would work in practice promised to be a complicated problem.

Proponents of switching to defined contribution plans generally argued that there would be budgetary savings. But they tended to neglect the most prominent feature of such plans; you actually have to contribute to them upfront. You have to have the cash on hand to make the contribution each year. You can't defer contributions. In contrast, the possibility of underfunding defined benefit plans gives budgeters some wiggle room in Bad Times. Moreover, switching from defined benefit to defined contribution does not erase the past liability under the old plan.[64]

In any event, legislative Republicans signaled that any budget deal that Governor Brown wanted them to endorse would have to include pension reform with some elements of 401k-type future benefits. As Republican State Senator Mimi Walters indicated, "We want reforms in place *before* there's any discussion about tax increases. I do know there's not support at all to even put it on the ballot without significant pension reforms."[65] (Italics added.) Along the way, Brown did offer pension changes. But from his perspective, the immediate state budget was largely unaffected by pension changes—since past accrued pension liabilities would have to be paid. Reducing benefits for new hires (and there would be relatively few new hires in the context of a budget crisis) or even benefits going forward for incumbent workers (if that were legal), would have little impact on the total cost to the state budget in 2011-12.

Generally, the Legislative Analyst favored a pension system that would be a hybrid of a defined benefit plan and a defined contribution plan for new hires. The state's Little Hoover Commission came out in favor of a reduced plan for new hires and—going forward—for incumbent workers and then testing the legality of that approach in court. A CalSTRS spokesperson termed the proposal "meaningless," arguing it was clearly illegal.[66]

Some version of a pension reduction plan might in theory have been negotiated with the governor by Republicans in exchange for a vote on tax extensions. But, as described below, there appeared to be no way to induce a tax extension vote, certainly not by June. However, via initiative, proposals to change public pensions could be put forth without action of the legislature. In a defensive move in early May public sector unions created "Californians for Retirement Security" to campaign against any pension ballot propositions that they disliked.

The pension issue led to dueling estimates of public sector pay vs. private.[67] Although proponents of reducing public pensions tended to point only to the pension element of compensation, a true comparison involves estimating total compensation (pay and benefits including pensions) in the public and private sectors. The differences in occupational mix between public and private employment must also be considered. It is clear that public employees generally have a larger fraction of their compensation in benefits than private employees. But if salaries and wages are lower for comparable public employees, total compensation might be roughly the same in the two sectors.

Although one study found total compensation a bit lower for public workers in California than private, and another a bit higher, there is enough uncertainty about the estimates to leave the precise answer undetermined. That is, the across-the-board public/private pay differential cannot be stated precisely but there is no evidence at the macro level of substantial over- or under-payment. However, there certainly are anecdotes and specific instances of abuses to

hold popular attention. Much attention was focused on the City of Bell in which the city manager was paid at outrageous levels and there were similar abuses regarding other city employees, notably the police chief.

There was no pension component to the eventual state budget deal reached in June since no deal on taxes was ever reached with legislative Republicans. Various union agreements negotiated at the state level increased employee pension contributions and provided some kind of two-tier arrangement with less generous pension provisions for new hires. (Similar agreements were bargained by local governments.) Various state-level pension initiatives were filed but—at this writing—none appeared to have the financial backing for a signature and election campaign.[68]

GETTING THERE: PART II—WORKING TOWARD THE DEADLINE

"It would be unconscionable to tell the electors of this state that they have no right to decide whether it is better to extend current tax statutes another five years or chop another $12 billion out of schools, public safety, our universities and our system of caring for the most vulnerable."

—Governor Jerry Brown 2011 State of the State address

"I don't understand why it is that the media has such a hard time with the idea that the people in (May) 2009 said no (to tax extensions)."

—Republican Senate leader Bob Dutton[69]

As Governor Brown's first month in office came to an end, he delivered his State of the State speech to the legislature which reiterated his call for Republicans to accede to his proposal for a special election on tax extensions. By then, about three weeks of the 60-day deadline he had given to the legislature to pass a budget (with the extension election) had elapsed. In the State of the State speech, he compared the call for democracy in Egypt (the "Arab spring" which had then erupted) with the need for a vote by Californians on tax extensions—a bit of a stretch.

Despite the rhetorical flourish, there was no sign that Republicans were becoming receptive to the placing of proposition on the ballot by June that would allow a vote on tax extensions. One factor that began to creep into the discussion was that revenues of the state—mainly from the personal income tax—were up 11% through January relative to the same period in the previous fiscal year.[70] Income taxes are very sensitive to developments in the upper tax brackets, especially capital gains. So they can be out of line with the underlying economy, depending on the incentives to sell stocks and other assets that have appreciated. Despite the erratic nature of such receipts, the more there was short-term good news on revenues, the less convincing was the argument for tax extensions.

To try to offset such impressions, legislative Democrats asked the Legislative Analyst Office (LAO) to come up with a "budget from Hell," since the governor hadn't explicitly provided one. The LAO presented suggestions for how such a budget might look and found hypothetical reductions of $13.5 billion.[71] But, of course, such an exercise was not a budget, or even a budget proposal. Budgets and budget proposals come from the governor and legislature, not the LAO, and must be politically feasible. Moreover, the LAO report was premised on the governor's revenue assumptions (and on the governor's insistence on a positive general fund balance by June 30, 2012). Some combination of added revenue—from a rising tax base, not extensions—or a less-strict ending point might avoid, or partly avoid, the budget from Hell in the LAO's example.

In any case, while Republicans talked with the governor and made public statements expressing their wish for various goals related to pensions and other items as the clock ticked. There was never a clear statement that votes would be provided for tax extensions to be placed on the ballot by the June deadline. GOP senate leader Bob Dutton said in mid-February that he was "not interested in providing any votes" and that "nobody (among legislative Republicans) has approached me and said they're willing to go in that direction."[72]

Despite such statements, Governor Brown appeared confident that a deal could be reached and seemed more concerned with the technical issues. For example, there was the question of whether the budget-related ballot issue could be posed as a single proposition or whether a series of budget-connected propositions would be needed. While Dutton was making his observations, Brown said he preferred a ballot offering that would be "clear and simple" but indicated that the details had yet to be decided.[73] (Ultimately, the title for the ballot proposal was to be named appealingly, the "Public Safety and Public Education Act of 2011.") In a joking reference to his former Jesuit training, Brown said he could grant Republican legislators who had taken a no-tax pledge a "dispensation" from their vow.[74]

The governor's dispensation remark was made in the context of an unusual hearing in which he testified at a legislative budget hearing. So Brown was clearly focusing on communicating with legislators of both parties. Relying on the governor's assurances that a tax extension deal could be reached, the Democrats in the legislature began to work on enacting the budget cuts that were contained in his January proposal. However, even if enacted, some of the cuts were not wholly within legislative control; Medi-Cal cuts, for example, might require federal approval.

Some proposals, while not needing federal government approval, might involve federal courts. The state—as noted—was under pressure to reduce prison enrollments—or spend more on prisons—as part of federal litigation. Part of Governor Brown's response to that pressure was to incorporate the prison issue into his proposal for realignment—the pushing of state functions down to the locals.

In the case of prisoners, realignment would move certain state prisoners into local jails. However, there was pushback from local officials who argued that county jails were already overcrowded and parole officers were already overburdened. As a result, the realignment proposal for prisoners had to be scaled back.

In other cases, there could be indirect effects of budget cuts. Tuition at UC and CSU might rise (and ultimately did), depending on the depth of the budget cuts. At a more conceptual level, UC-Berkeley's chancellor indicated that his campus had effectively gone from being a "state-supported university to a state-located university." With state support diminishing and increased reliance of federal research funds, he asserted that UC-Berkeley could be described as a federal institution.[75] Apart from abstract concepts, to varying degrees, UC campuses moved toward acceptance of more out-of-state residents who pay full tuition as a source of revenue. Campus layoffs were also announced.

GETTING THERE: PART III THE DEADLINE PASSES

"I meet with them all the time, night and day."

—Governor Jerry Brown asked if he is meeting with Republicans a week before his 60-day deadline expired[76]

As the 60-day deadline Brown had set for the legislature to pass a budget and put tax extensions on the ballot approached, there was no sign of the latter happening. The needed Republican votes were still lacking. The governor worked on rounding up business support, hoping Republicans would respond to the business community. As noted earlier, the state Chamber of Commerce did not exactly endorse the specifics of his plan but hinted that a deal which included comprehensive reform (essentially other items such as pensions) would be supported. The Bay Area Council was more explicit in supporting the governor's plan, as was the Silicon Valley Leadership Group. Business groups in the Los Angeles area also gave support. But from the conservative Howard Jarvis, such business support was characterized as "appeasement" of legislative Democrats.[77]

Brown continued to believe that he could garner a few needed Republican votes and suggested that the 60-day deadline might have to slip a bit. However, on March 7, five Republican legislators—the "Gang of Five"—sent a polite letter to the governor saying that since their proposals for "real reform" were evidently not acceptable, the talks had "reached an impasse."[78] Their proposals—the precise wording of which was never completely clear—were developed with the advice of two fiscal consultants, one of whom, Mike Genest, was a past budget director of Governor Schwarzenegger and who was also connected to groups pushing for public pension cuts.

Meanwhile, the governor's relationship with Republicans took on a testy edge. The chair of the State Republican Party offered Brown an invitation to debate Grover Norquist—author of the no-tax pledge that many legislative Republicans had signed. Brown, who had criticized Norquist as an out-of-state interferer with California democracy, declined the invitation but offered to send his dog Sutter instead for such a debate. And on March 10, Day 60—the official deadline day—came and went without a deal.

A few days later at a Republican state convention, the conservative California Republican Assembly faction pushed to label any Party legislators who voted for Brown's proposed tax extension ballot measure as "traitorous."[79] (A resolution to that effect was never passed.) At around that time, Republican legislators who had been in talks with Brown added relaxation of various environmental rules to their terms for a deal, i.e., issues that were not directly connected to fiscal affairs. Such a deal would have been particularly difficult for Brown since voters had rejected an attempt to relax environmental rules the previous November.

By mid-March, the legislator had approved a modified version of Brown's spending plan, i.e., with cuts at a level that still assumed revenue from tax extensions would be forthcoming. In some instances, however, Republican votes were not forthcoming for the cuts. Brown complained that "they don't want to balance the budget with cuts. And they don't appear to want to balance it with new revenues. So they must want a profound, continuing unbalanced budget."[80] And he continued to predict there would be a ballot measure "one way or another."[81]

Such complaints and predictions, however, did not produce the needed Republican votes for a ballot measure on tax extensions. And, from a purely administrative perspective, it was becoming doubtful that a special election could be held by June. Still, Brown did not concede that the deadline had truly

passed. "We'll know the deadline when we've passed it," he said cryptically.[82]

Apart from the issue of obtaining Republican votes for tax extensions, the redevelopment agency issue remained in a limbo of one-sided negotiations with local governments threatening lawsuits and, alternatively, compromises. There were also threats that even if the legislation proposed to abolish the agencies allowed payments of past debts, the mechanism created to enable such payoffs would be legally questionable and open local government to lawsuits by agency creditors. The redevelopment issue also split organized labor, an important Democratic Party constituent.

The California Teachers Association (CTA) and Service Employees International Union (SEIU) Local 1000 favored abolishing the agencies because of the added resources abolition would generate for the state budget. (Schools are heavily dependent on state budget aid and SEIU 1000 represents state workers who had an obvious interest in aiding the budget.) AFSCME, with significant local government membership, and construction unions, which liked the jobs redevelopment creates, opposed abolition.[83] Meanwhile, in the rush to grandfather new projects, the agencies were reported to have floated at least $770 million in new bonds from January through late March.[84]

The issues of a ballot measure, redevelopment, and unions were linked. With the clock ticking, the governor began to hint at a November 2011 special election rather than one in June. Were that to occur, the tax *extensions* would by then become tax *increases* and would thus face a much higher hurdle for voter approval. (Alternatively, the taxes could be extended until the election, something Republicans would be very unlikely to support.)

Funding for a campaign to pass such a proposition would have to come largely from organized labor. However, there might be time to put a tax proposition (or propositions) on the ballot in November via petition, i.e., without Republican votes. Thus, hints of a November strategy could have been a tactic to indicate to Republicans that they had less leverage than they thought.

But if organized labor was not amenable to funding such an uphill fight—and was split on redevelopment—the tactic was not credible unless there was some other source of money. It was noted that Brown had $4 million left over from the gubernatorial election to put into a November initiative approach. That sum was more than enough to round up the needed petition signatures. But it was not enough, absent some other funder, to handle a campaign.

Brown was winding up contract negotiations with various state unions by late March which might have made them more willing to fund a campaign. But funding was still an issue. Unions would not want to invest what could be tens of millions of dollars into a fight that might well be unsuccessful.

Republicans could also make strategic gestures. They pointed to liberal New York Governor Andrew Cuomo who was signing off on an early state budget without tax increases. Brown should do the same, was the argument. In late March, two initiatives were filed on the behalf of legislative Republicans. One was a pension measure that seemed loosely modeled on the Little Hoover Commission recommendations. The other was a formula-based spending cap, effectively designed to revive the old Gann limit, a spending cap which voters approved in 1979 but which they later effectively gutted.

These measures—viewed as a tactic—also had limits. The last time a spending cap was on the ballot in 2005, it was decisively rejected. Earlier such propositions had been rejected under Governors Pete Wilson and Ronald Reagan.[85]

The public response to a pension initiative was also not predetermined. Sacramento politicos and media types tended to assume that cutting public pensions was an automatic winner. And media reports on opinion polls tended to foster that view. It was true that if voters were given a menu of pension cutbacks as hypothetical reforms, they tended to support them, as the March 2011 California Field Poll reported. After all, if a pollster is asking you about reforms, you tend to assume reforms must be needed. Why else would the questions be posed?

But the same Field Poll indicated—although news media seemed to miss the point—that more voters thought public pensions were "about right" or "not generous enough" (48%) than thought they were "too generous" (42%).[86] And this surprising result appeared after well over a year of media reports on pension underfunding and particular abuses.

Still, however these actions and statements by Republicans and the governor are interpreted, there was an underlying fact that ultimately determined the outcome. From the Republican standpoint, talking with the governor and letting the clock run was a winning strategy. Although the exact deadline was never clear, eventually there would be no possibility of a June election and tax extensions would become tax increases if they were then offered to the public. Increases would be tough to pass. For precisely that reason, the increase option might never be offered at all. Republicans could then point to the fact that they were opposed to tax increases or extensions and prevented them from happening.

GETTING THERE PART IV: APPROACHING THE MAY REVISE

"What now? Nobody knows. 'Exploring all our options,' Brown and Democratic leaders are saying. But there is no Plan B."

—Columnist George Skelton[87]

"...I'm going to go up and down the state to see if I can't hug Republicans and... tell them, 'We love you, but give us a break. Let the people vote.'"

—Governor Jerry Brown[88]

If Brown had succeeded with his original 60-day time frame, the standard operating procedure of state budgeting would have changed. Normally, governors submit their constitutionally-mandated budget proposal in January. And normally, although hearings are held, the legislature does not enact that budget before June (and sometimes much later). In May, by tradition, the governor submits the "May Revise," a modified budget proposal that reflects both an economic update (forecasts of revenue, etc.) and a political update (what seems able to be passed). By the beginning of April, it was apparent there would be a May Revise.

Given the general economic climate of the state and the fact that the original budget plan seemed stalled, Governor Brown was doing reasonably well in the public eye. The Field Poll for March found his approval ratings among registered voters at 48%, disapproval at 21%, and 31% in the "no opinion" category. That is, most voters either still thought positively of the governor or at least were withholding judgment. In contrast, when Brown in his previous incarnation as governor left a budget crisis to his successor, George Deukmejian in 1973, Deukmejian's ratings were 42-28-30%. By that measure, Brown was

doing somewhat better than his earlier predecessor, in roughly the same position.[89]

There are no polls on public attitudes specifically regarding those Republicans in negotiations with the governor. But one—Senator Bob Dutton—ended up looking silly when he complained that during the negotiations, he was "yelled at" by Anne Gust, Brown's wife and advisor.[90] A Brown spokesperson joked that the governor's dog also barked at Dutton. Brown said that Dutton was "filibustering" and that Gust had "some level of impatience for that kind of nonsense."[91]

In any event, whatever the public attitude might have been toward Dutton and his complaints about the first lady (and possibly the first dog), the legislature as a whole was very poorly regarded relative to the governor among voters: 16% approve, 70% disapprove, 14% no opinion. Embroiling itself in a controversy over regulating shark fin soup in the midst of a budget crisis did not improve the legislature's image. Not long after the yelling episode, a state panel voted to eliminate the purchase of cars for legislators, substituting a less-costly transportation allowance.

Although exactly what would be in the May Revise was not known, there was preemptive litigation filed. Some "First Five" local commissions—who receive earmarked tax revenue approved by voters—filed suit against a potential taking of that revenue by the state.[92] There had already been cuts in such programs pursuant to earlier raids on First Five funds and there would be more to come.[93] UC-San Diego postponed the establishment of a new law school due to "the state's changing fiscal picture."[94] UCLA's chancellor wrote an op-ed noting that the 29 members of the Republican legislative delegation had attended California higher education institutions but were unwilling to provide a vote that would avoid greater cuts to those institutions.[95]

K-12 teachers and other groups protested at the Capitol. The California Teachers Association oddly pushed for Brown somehow to enact tax extensions without a ballot measure. How he was supposed to produce such a result was a mystery.[96] If he did not have a two-thirds vote for a ballot measure, he certainly did not have it for tax extensions. CTA also ran TV ads urging the legislature to pass a budget, presumably with tax extensions and without an election on the issue. The governor continued to negotiate concessionary contracts with state labor unions but the Legislative Analyst questioned the magnitude of the savings achieved and Republicans threatened to vote against approval of the agreements.

Various budget scenarios were aired. At one point, the governor indicated he might present a budget that assumed that there would be tax extensions on the ballot and that they would pass, even if the votes for such developments had not yet happened.[97] Democrats floated new tax ideas—such as a tax on sugary sodas—but then dropped them since Republican votes were not available for passage. Treasurer Bill Lockyer opined that maybe if an all-cuts budget had to be passed, the cuts should be concentrated in Republican districts. "The people who want less government ought to be at the front of that line to get less government," he said.[98]

Senate leader Darrell Steinberg mused that perhaps children in Republican districts could be spared from disproportionate targeted cuts but perhaps adult services could be considered.[99] Although targeting was denied, a redirection of vehicle license fee (car tax) money contained in the eventual budget particularly hit certain Republican districts. A spokesperson for the governor, commenting on the impact on particular Riverside cities with Republican representatives noted that residents there could "thank (their) legislators for their predicament."[100]

There were symbolic moves as the date for the May Revise approached, such as cutbacks in travel by state workers. And there were practical administrative problems. If the extension of the Vehicle License Fee (car tax) did not occur, the tax rate would fall on July 1. The Department of Motor Vehicles (DMV) would normally have started sending out bills for license renewal due in July 60 days in advance. By legislative action, the sending out of DMV bills was delayed, causing subsequent confusion about renewals over the summer. There was also a move—ultimately not carried out in the face of considerable opposition—to enact a bill giving local governments more authority to raise local taxes. The idea was that if there was going to be realignment—pushing programs down to the locals—the locals should have more control of their own revenues.

Shortly before the May Revise was released, state receipts of tax revenue in excess of projections through April were reported. Compared with the estimates in January for the 2010-11 fiscal year ending in April, an additional $1.3 billion had been received, about $300 million extra in just the month of April.[101] The initial reaction of the Brown administration was to downplay the uptick and to point to a variety of reasons why the revenue bump did not solve the budget problem. Indeed, a list of seventy state parks that might be closed was issued.

However, GOP assembly leader Connie Conway, saying "schools should be first," pointed to the uptick as a solution to K-12 funding issues, a viewpoint that would undermine Brown's tax proposals.[102] And, as it turned out, the uptick essentially became a major element in the eventual enacted budget which depended on optimistic economic/revenue projections. But in early May, the governor still hoped that some kind of tax extension/increase would materialize.

Republicans, however, issued budget proposals just prior to release of the May Revise that included no tax extensions. And word was then passed to the media that the governor's May Revise would drop extension of the personal income tax surcharge for one year and would maintain only the sales tax and vehicle license fee extensions for immediate (July 1, 2011) continuance. The new plan would ask the legislature (which meant some Republicans to obtain the two-thirds necessary) to extend the two taxes until a measure could be put on the ballot in the fall asking voters for retroactive approval.

That position put Governor Brown at odds with legislative Democrats who were not anxious for any election to be held. Assembly leader Steinberg said that the election should be "as far off as is reasonably possible."[103] How approval for the tax proposals—even scaled back—with or without an election was to be obtained absent a two-thirds vote was not made clear by Steinberg or others promoting that path.

THE MAY REVISE

"(T)he May Revise goes too far on taxes and not far enough on reforms."

—Senate Republican leader Bob Dutton

"This proposal... reflects our commitment to a balanced approach... which is why the Governor is calling for revenue extensions..."

—Assembly Speaker John Pérez[104]

Apart from scaling back the original January proposal on extending the income tax surcharge, the May Revise included various business tax breaks—something presumably attractive to Republican legislators. It also included elimination of various state commissions and other entities and reductions in the state workforce. Within broad spending categories, there were many reallocations with some programs proposed to receive more than in January and others less.

As to the idea of a vote on tax extensions, by June the governor could cite a PPIC poll indicating that over

60% of voters favored having such an election.[105] The California Field poll—in contrast—showed continuing support for the election idea but only by a plurality.[106] Differences between the two polls illustrate the impact that reasonable variations in survey methodology and question formatting can have on poll responses.

Table 6 summarizes the highlights of the May Revise in comparison to the earlier January proposal. One of the oddities is that the General Fund was said to have had a negative reserve as of the previous July 1, 2010 in May that was about $1.6 higher than had been reported in January. This revision of history appears to have been largely a change in accounting and is the kind of looseness in state budgeting that clouds the fiscal situation. In theory, the use of accrual accounting by the state should improve understanding of underlying trends. But in practice it appears to open the door to data obscurity and public disdain.

Table 6: The May 2011 (May Revise) Budget Proposal ($ millions)

	Governor: Jan. 2011 Proposal 2010-2011*	Governor: May 2011 Enacted to Date 2010-2011	Governor: May 2011 Proposal 2010-2011
Fund Balance Start of Year	-$5,342	-$6,950	-$6,950
Revenue & Transfers	$94,174	$94,477	$95,740
Expenditures	$92,209	$91,693	$91,566
Surplus/Deficit	+1,985	-$2,106	+$4,174
Fund Balance End of Year	-$3,357	-$4,166	-$2,776
	2011-2012*	**2011-2012**	**2011-2012**
Fund Balance Start of Year	-$3,357	-$4,166	-$2,776
Revenue & Transfers	$89,696	$89,867	$93,623
Expenditures	$84,614	$96,888	$88,803
Surplus/Deficit	+$5,082	-$7,021	+$4,820
Fund Balance End of Year	+$1,725	-$11,957	+2,044

*Same as Table 5.

Source: California Governor, *2011-12 Governor's Budget: May Revision*, May 2011.

If the focus is just on expenditures and revenues (and transfers), there is in fact little difference between the flows for the then-current 2010-11 fiscal year between January and May. In January, the General Fund was projected to have a negative reserve of about -$3 billion at the end of 2010-11. Absent any changes beyond what had already been done since January (mainly cuts), the negative reserve by June 30, 2011 would have been about -$4 billion. With the governor's proposal, the negative reserve drops back to -$3 billion. However, with the 2010-11 year almost up, it was to be expected that the big changes would come in the following year.

For 2011-12, absent any major legislative action on the revenue side, revenue for 2011-12 was nonetheless projected to be about the same as the governor had proposed in January. In effect, therefore, a more optimistic forecast was making up for revenues that might have been lost due to not having tax extensions in place. Expenditures—absent more changes (cuts) that had already occurred—would still rise substantially by about $12 billion relative to the January proposal. With further cuts, the increase would only be about $4 billion. If everything the governor proposed in May and forecast in May were to come to pass, the state would run a $4 billion surplus in 2010-11 and close to $5 billion in 2011-12, leave a positive reserve in the General Fund at the end of 2011-12 of about +$2 billion, roughly his January target.

But these numbers all depended on Republican acquiescence to a tax vote and assumed voters would approve the ballot proposals. Yet there were no signs of forthcoming Republican support. A few days after releasing the May Revise, the governor said on that issue that "things (were) more positive than they were" in his discussions with Republicans "but we're not there yet."[107] This pattern continued until it finally became clear that no such support was going to be had, regardless of what the governor might feasibly offer.

Basically, what transpired was on-and-off negotiations, glimmers of hope, and an increasing sense among legislative Democrats that the governor was not going to succeed in obtaining his tax extensions, either by direct vote of the legislature or through some ballot measure that would require a two-thirds vote. Brown could in principle have used the initiative process for his ballot measure but no moves were made in that direction. But had he taken that route, it was unclear that he would have had the financial support needed to do a complete campaign tax proposition.

However, with the governor negotiating with Republicans and giving assurances that something would arise from his talks, the possibility that the legislature would miss the June 15 constitutional deadline to pass a budget increasingly arose. The longer legislators awaited a deal, the closer they got to June 15 without a budget plan ready to go. And under Prop 25 of November 2010—which gave the legislature the power to pass budgets (but not taxes)—by a simple majority, there was included a penalty if it did not meet the June 15 deadline to do so.

Each day without a budget would mean that a day's pay for legislators would be forfeited. Since the legislature had passed a partial budget (the cuts side), there was some argument that it had already met its constitutional duty.[108] That argument was pooh-poohed, however, if not from a legal analysis, then from a political viewpoint. Voters would be furious if what seemed to be the clear penalty of Prop 25 was circumvented.

Although the already-enacted partial budget would not pass muster to avoid the penalty, the legislature could pass a budget that "balanced" on paper by June 15 even if not in its eventual outcome. That approach would seem under Prop 25 to satisfy the requirement for timely passage. "Balance" was more a matter of doing the sums correctly than doing them realistically.

But even doing the sums correctly is not as simple as writing numbers on a sheet of paper. There are budget formulas that have to be followed, such as the Prop 98 requirements for K-14 funding. And there are typically pieces of the budget—trailer bills—that are inherent in the overall budget design but are passed after the basic document. All of these features of budgeting were to come into focus in mid-June.

ENACTING THE BUDGET: PART I—THE FIRST ATTEMPT

"In passing Proposition 25 last November, voters clearly stated they expect their representatives to make the difficult decisions needed... by the mandatory deadline or be penalized. I will enforce the voters' demand."

—State Controller John Chiang stating he would not pay legislators for days after June 15 until they had passed a "balanced" budget[109]

"I now have to explain to my wife and daughter that we won't be able to pay the bills because a politician chose to grandstand at our expense. California has officially degenerated into a Banana Republic..."

—Assemblyman Mike Gatto complaining about losing pay due to the Controller's action[110]

Various developments occurred after the release of the May Revise. Some events seemed helpful for eventual passage. For example, the U.S. Supreme Court ruled against the state on the issue of prisoner releases. Short of just letting prisoners out, the state would have to follow through on its plan to move some of them to local jails. Governor Brown indicated he would ask the lower court for more time to accommodate. But even that approach would require funding from the state to the counties for the costs, and thus seemingly supported the need for tax extensions. However, beyond the issuance of GOP statements criticizing the Court, there was no indication that Republicans were

more favorable to tax extensions after the decision than before.

In addition, although a pension initiative had been earlier filed by Republican legislators, shortly after the May Revise was released, they indicated they would not be circulating the initiative. At the time it was filed, the pension initiative had been seen as a negotiating tactic to pressure the governor and the Democrats. By making no effort to pursue the initiative, the Republican message seemed to be that negotiations on tax extensions were effectively over, i.e., they would not agree to extensions or a related ballot proposition. Indeed, they made the message explicit.

Republican assemblyman Roger Niello—the official sponsor of the initiative—said in explaining the decision not to circulate, "The reason for filing this measure was to have something in line for a November election alongside the measure on taxes, but that appears unlikely to happen now."[111] Still, in early June, the governor still was indicating that a deal with Republicans was in reach. "There's compromises and discussion going on," he said.[112]

As it turned out, however, the deal that Republicans were ostensibly willing to consider would have let the temporary taxes lapse on July 1 and then had an election on whether voters would like to raise them back up. That formula was very likely to produce a voter rejection. Brown by that time was saying that apart from that issue, he was prepared to offer pension changes, a spending cap formula, and regulatory relaxations in exchange for a ballot proposition on taxes, so long as there was a "bridge tax" (an extension of the temporary taxes) until the election.

There was some confusion in reports as to whether Brown was pushing for a 3-month or 6-month bridge; at one point even a 12-month bridge was written into a draft of the budget. However, Republican Senator Bob Huff indicated that "there's no Republican votes for a temporary tax," i.e., the bridge tax was not acceptable.[113] And unions indicated that they did not want to throw money at a campaign for approving tax extensions that would be "fraught with peril" and would likely fail.[114]

With a week to go before the June 15 deadline, the Democratic leadership in the legislature decided to go ahead and pass a budget without waiting any longer for a deal between the governor and legislative Republicans. The only move the Democrats took toward trying to provide some incentive for Republican cooperation was to advance the bill allowing local governments more leeway in raising local taxes. Evidently, it was thought that Republicans would not want such authority bestowed on the locals. And, indeed, GOP legislators termed that bill "another club to use over Republicans."[115] But they did not acquiesce on the bridge-tax/ballot issue despite the "club."

Putting together a budget is a complicated process and a hasty effort to meet a deadline might produce a technically flawed plan. However, legislators seemed to believe that if they passed something by June 15, that action would satisfy Prop 25 and that flaws could be corrected later. The rapid push for enacting a budget seemed to open the door to provisions that might have been differently crafted had more time been available. For example, nursing homes managed to obtain more favorable treatment—given that there would be Medi-Cal cuts—than other health providers, provoking complaints.[116] A legally questionable element was included that would effectively retain the temporary sales tax surcharge. There was also a revival of the dubious Schwarzenegger plan to sell and lease back state office buildings—which Governor Brown had previously rejected.

Tensions rose as the June 15 deadline neared. A near fight in the assembly between a Democratic and a

Republican legislator—ostensibly over a slur against Italian-Americans—was averted as other members separated the two. At the end, a budget was passed within the deadline which Senate leader Darrell Steinberg termed "not perfect. It is Plan B... worthy of the governor's signature."[117]

However, Plan B, as Steinberg had dubbed it, didn't get that signature. The governor had posted a YouTube video about the status of his budget negotiations and told the news media—two days before the June 15 deadline—that the budget was in "a fuzzy zone that's not yet been transcended."[118] But he did not say what he would do with the budget bill legislative Democrats were preparing that was already near completion, perhaps suggesting to them erroneously that he would sign their budget.

However, the day after the budget was passed, Governor Brown vetoed the entire deal "for the first time in history," as he declared. In another YouTube message, he said the budget he had been sent was "not a balanced solution" and was "not financeable."[119] Brown still called upon Republicans to approve his tax extensions. He hinted that he might go the initiative route to circumvent Republican opposition, although that threat—given the explicit and public reluctance of labor unions to finance such an effort—was rather hollow.[120]

There was some support from the business community expressed for the initiative approach in an effort to back up the governor.[121] But putting together a coalition willing to finance an initiative campaign with a large chance of voter failure would have been difficult. And, if proof were needed, it did not happen despite continued refusal by Republicans to back a tax-extension/bridge-tax ballot measure.

Still, Brown's veto was greeted enthusiastically for the drama of it and the governor became a media hero. The veto submerged criticism that the governor—by holding out for almost 5½ months the prospect of an eventual deal with Republicans that never occurred—had set the stage for the last-minute, slap-dash budget he was then rejecting. The legislature had held off its budget drafting because the governor kept assuring its Democratic leaders that such a deal could be made.

If Brown was a media hero, Senate President Darrell Steinberg seemed to be looking to be cast as the anti-hero. The day Brown announced his budget veto, Steinberg responded that the senate would not consider confirming gubernatorial appointees "for an indefinite period," a statement that appeared spiteful.[122] Oddly, there was only one such Brown appointee in the hopper; most of those awaiting confirmation were holdovers from the Schwarzenegger administration. So the holdup in confirmations was not much of a threat.

Although Steinberg explained the confirmation holdup as the result of a need to concentrate the senate on budgetary matters, Brown took it as retaliation but characterized the move "as a small price to pay" (which indeed it was).[123] Steinberg also raised legal issues about the withholding of pay and characterized the controller's action as "dangerous."[124] The problem was that such arguments were really against Prop 25 which voters had approved.

And it was—in any case—impossible for a legislator to complain about the pay forfeiture without appearing to be self-serving. There were complaints from the Republican side that the pay forfeiture was an attempt to make them "compromise values." But Republican legislators were not in a position to be heroes except within their constituencies.[125]

With a hero and an anti-hero in place, there was room for a second hero to step forward. Treasurer Bill Lockyer agreed with the governor that the budget was "not financeable."[126] He estimated that the state would need to borrow $7 billion during the 2011-12

fiscal year but believed it would not be able to repay by the end of the year. While Lockyer's concurrence was noted in news reports, it lacked the drama of a veto and was too technical in nature for him to become a media hero. In any event, the treasurer had no immediate role in the process and could only opine.

The controller—in contrast—had a more direct role. Even though the governor vetoed the budget, the legislature had enacted it by the June 15 deadline. State Controller John Chiang—as the state's official paycheck writer—had earlier declared that he would make a judgment about whether legislators should be paid pursuant to Prop 25 if they had not passed what he interpreted to be a "balanced" budget by June 15. So the issue became whether the controller viewed the vetoed budget—which was passed on time—as meeting his definition of balanced, even if it had not met the governor's.

Chiang set the stage for making a technical decision that could nonetheless be seen as heroic. A spokesperson for his office noted that "balance" did not mean realistic, in the sense that revenues were likely to be what they were projected to be in the budget. Instead, "balance" meant that the calculations were in some sense correct so that *assuming the projected revenues would be there*, the expenditures would be in sync.

One hurdle the vetoed budget might have to surmount, under Chiang's approach, was Prop 98 with its formula-based budgeting for K-14. If Prop 98 was not properly followed, that error would allow Chiang to rule that the vetoed budget was not balanced and that he therefore would not/could not pay legislative salaries. But he could still rule that some subsequent budget that might be optimistic about revenues but had the sums done right would meet the standard.

Chiang could therefore take a stand against an errant and unpopular legislature whose budget the governor had already tanked, so long as he could find a technical mistake in the vetoed budget. Put another way, the balanced-only-if-the-sums-are-done-right approach would not force the controller into some later confrontation with the governor who might have to sign an optimistic budget in the end if no Republican votes for tax extensions materialized. (Chiang later indicated that if a budget were signed by the governor, the controller would have no role in deciding if Prop 25's requirements had been met.)

On June 21, five days after the budget veto, Chiang announced in a media release that the vetoed budget "did not balance on paper." Policy wonks understood that "on paper" meant only that, given the assumptions in the budget, there were technical errors in drafting, the largest being problems of compliance with Prop 98. Other errors found by the controller involved revenues that would require subsequent legislation—legislation that had not been passed by June 15. All of these errors, which totaled less than $2 billion according to the controller, could have been "fixed" by getting the sums right and a more optimistic—though not necessarily realistic—revenue forecast.

But this point was lost on TV versions of what had happened. Chiang became a hero, even on Fox News, which rarely finds heroes among Democrats, because he struck a blow at the legislature. The conservative Howard Jarvis Taxpayers Association declared that "as lawmakers now threaten to sue the State Controller" it "stands behind Chiang in his decision."[127]

On the other hand, from the Democratic side, there came the Hollywood equivalent of "you'll never have lunch in this town again." Assembly leader Charles Calderon said Chiang had "facilitated" a "freak show."[128] Only a year before, Chiang had been a Democratic hero by refusing to cut the pay of state workers to the minimum wage—again, on technical grounds—during a budget stalemate with Governor Schwarzenegger. But his past glories (among Democrats) were forgotten when it meant a pay forfeiture.

ENACTING A BUDGET: PART II—SUCCESS OF SORTS

"This budget is the most austere fiscal blueprint California has seen in more than a generation... Unfortunately, Democrats were forced to deliver alone..."

—Senate President Darrell Steinberg[129]

"Republicans listened to the voters and stayed true to the only special interest we represent—California's taxpayers."

—Assembly Republican leader Connie Conway[130]

By late June, the governor had come to the conclusion that no Republican support was going to be obtained for his tax extensions. Legislative Democrats had come to that conclusion earlier. The idea—pushed by some unions—that the legislature should somehow pass a budget with taxes but no ballot measure (even though a two-thirds vote was needed either way) had been dropped. Controller Chiang had made himself unpopular with legislators—not with the public—but the controller has no role in formulating budget bills.

Governor Brown had also made himself unpopular with legislative Democrats because of his veto of the June 15 budget. But—unlike the controller—without the governor, there could be no budget. So legislative Democrats and the governor inevitably had to craft a budget that could be passed by majority vote and that would not be vetoed. Such a budget might have some elements of revenue enhancements but could not increase or extend taxes. And the ability to raise many fees was now constrained by voter action in November 2010.

On June 27, a new deal was announced, one the governor would sign. In a meeting with the news media, Senate President Steinberg, Assembly speaker Pérez, and Governor Brown appeared together—all appearing friendly—and outlined the details. There was reference to some future initiative on revenues—but it was vague and not part of the 2011-12 budget. In a press release, Steinberg put the date of a possible initiative at November 2012. That date would not even be the first available state election or within the 2011-12 fiscal year. (The state and presidential primary would come earlier: in June at the end of the fiscal year.)

Essentially, the 2011-12 budget was of the "all-cuts" type but with optimistic assumptions on revenue—roughly the optimistic assumptions (a bit less) that had been presented in the May Revise absent the tax extensions. However, as **Table 7** shows, about $5 billion in revenue had to be subtracted from the May Revise because of no tax extensions were included. Expenditures were down about $3 billion from the May Revise so the ending reserve in the General Fund, while positive, was a razor-thin $1 billion.[131]

Table 7: The June Enacted Budget Proposal ($ millions)

	Governor: May 2011 Enacted to May 2010-2011*	Governor: May 2011 Proposal 2010-2011*	Enacted June 2011 including Vetoes 2010-2011
Fund Balance Start of Year	-$6,950	-$6,950	-$4,507
Revenue & Transfers	$94,477	$95,740	$94,781
Expenditures	$91,693	$91,566	$91,480
Surplus/Deficit	+$2,784	+$4,174	+$3,301
Fund Balance End of Year	-$4,166	-$2,776	-$1,206
	2011-2012*	**2011-2012**	**2011-2012**
Fund Balance Start of Year	-$4,166	-$2,776	-$1,206
Revenue & Transfers	$89,867	$93,623	$88,456
Expenditures	$96,888	$88,803	$85,937
Surplus/Deficit	-$7,021	+$4,820	+2,519
Fund Balance End of Year	-$11,957	+2,044	+1,313

*Same as Table 6.

Source: California Governor, *2011-12 State Budget*, June 2011.

Since the governor was originally committed—he felt—to ending the new fiscal year with a positive reserve, any fall off in revenue relative to assumptions could tip into negativity. Seemingly to avoid that outcome, the budget contained a trigger of more cuts should revenue fall short by a specified margin. As described below, the trigger did not actually guarantee a non-negative reserve.

To justify the optimism on revenues in June, there turned out to be about a $1 billion more revenue received for the 2010-11 fiscal year that was coming to an end than had been included in the May Revise. (That figure was not officially known at the time the new budget was prepared but undoubtedly there were some preliminary figures available to the Department of Finance.) And, as previously noted, the May Revise itself reflected receipts above the January projections. The difficulty was that the underlying state economy was not performing well which could indicate the improved revenue results were transitory.

The January assumption on revenue, absent tax extensions, for 2011-12 was about $83.5 billion. (**Table 4**) The June assumption was $88.4 billion. There was some revenue enhancement in the June budget from the "Amazon tax" (requirement that out-of-state retailers remit sales tax), a rural fire fighting fee, and a car-related fee. So something like an extra $4-$5 billion in revenue was being assumed relative to January.

Among the more publicized cuts were those to UC and CSU—with still more chops planned if the trigger were pulled. Both systems quickly raised tuition in response. But other programs in the social welfare area also were hit that received news media attention. The temporary taxes the governor originally wanted to extend lapsed. And with the budget enacted and the spotlight off the legislature, five legislative Republicans requested that the attorney general review whether controller Chiang had acted legally in cutting off legislators' pay.

As for the trigger, it was actually a two-part affair. If revenues fell below projections by $1-$2 billion—as certified by the Department of Finance in mid-December, there would be a programmed cut in various programs (including, as noted above, higher education) of $600 million. If the revenues were below projections by more than $2 billion, another $1.9 billion would be cut, heavily from K-12.[132] The cuts would take effect on January 1, 2012, half way through the fiscal year. The trigger mechanism would not in fact insure that the General Fund would have a non-negative reserve at the end of fiscal 2011-12, although it would provide some downward cushion.

Of course, the legislature could act at any time during the fiscal year to modify the trigger. And while the trigger was to be pulled if revenues fell short of expectations, there was no trigger if expenditures were higher than projected. So even the cushion's impact was not a certainty. Nonetheless, Treasurer Lockyer now pronounced the budget to be "financeable."[133]

AFTERMATH AND OUTLOOK

"...(O)bsessive, partisan ideology is what's making it impossible to govern."

—Governor Jerry Brown[134]

As noted, in the aftermath of the final budget passage, UC and CSU tuitions were quickly raised, although not to the level the governor had suggested could occur under an all-cuts budget when he was still officially hopeful about ultimately obtaining tax extensions.[135] Referenda petitions were filed to block the "Amazon tax"—the new law requiring out-of-state retailers to collect and remit California sales tax—the fee imposed to finance rural fire fighting, and a complex budget

deal on redevelopment agencies.[136] A bill designed to make it more difficult to gather signatures for ballot measures might have impeded these efforts, but was vetoed by the governor.[137] With the veto, that potential impediment was removed.

A radio ad paid for by labor unions told listeners that signing petitions (any ballot petitions) opened them up to identify theft.[138] Despite the potential hurdle the ad might engender, it seemed likely that the budget-related referenda—certainly the Amazon tax—would make it to the ballot. Early on, Amazon contributed enough money to the campaign to obtain the needed signatures.

When enough signatures for a referendum are obtained to put it on the ballot, the law targeted is blocked until the election.[139] Thus, even if voters reject the referendum's proposal to repeal a law in a later election, revenue that might have been collected is lost in the interim. And, of course, if they vote for repeal, even more revenue is lost. The referenda, in short, represented a downside risk for the state budget.

Legal and other challenges to budgetary components represented a similar one-sided risk. At this writing, a court challenge to the budget's redevelopment agency provisions has been filed. A court decision on Indian gambling revenues threatened a portion of that source of funds.[140] Health providers are challenging a waiver the state is seeking from the federal government for its Medi-Cal savings. A group of Assembly Republicans have asked the attorney general to opine on whether Prop 98's funding guarantee is being satisfied by the new budget.[141]

If a revenue element of the budget is challenged in court or elsewhere, the challenge will either succeed or fail. If it fails, the budget is no better off than it was projected to be. If the challenge succeeds, there is less revenue. Similarly, if there is a legal challenge on the spending side, the claim is typically that not enough is being spent to meet some requirement, say, for federal matching funds. If the challenge succeeds, more will be spent than projected. If it fails, the budget proceeds as it was written. So in the legal realm, as in the electoral realm, the risk to the budget is all in the direction of deterioration, not improvement.[142]

In a sense, the Washington debt-ceiling negotiations during summer 2011 had elements of the Sacramento drama. Governor Brown didn't come to a conclusion until just before the deadline for a new budget that a tax deal was not going to be possible with legislative Republicans. Similarly, President Obama seemed to believe—despite the earlier California lesson—that a compromise with "tea party" Republicans involving increased federal revenue might be had. However, debt-ceiling negotiations and the eventual deal on that subject in Washington at the August 2 deadline echoed back to California in a two-part risk for the state's budget. As in Sacramento, there was little sign of a compromise in Washington.

The debt-ceiling deal of August 2011 had the potential to slow the U.S. economy which already was performing poorly. A U.S. slowdown would be reflected in the state's economy and adversely affect the tax revenues that had been (optimistically) projected for the 2011-12 budget. In addition, various federal funds that flow to California could be reduced or ended. These funds—to the extent that they flow to the state—often affect budgetary categories outside the General Fund for programs such as unemployment benefits and other social welfare objectives. But to the extent they cut federal support in those areas, there would be pressure for state and local governments in California to pick up some of the resulting gap.

Given the downside risk and the trigger provision built into the 2011-12 budget in case of revenue falling below projections, the budget decisions of June 2011 might well have to be revisited as part of a midyear correction. What might happen in such a

revisit is uncertain. But it seems unlikely, given his on-the-job learning update in bipartisan compromise, that Governor Brown will again spend anywhere near the time and effort he did during the first six months of 2011 trying to reach a deal with the minority party.

ENDNOTES

1 This chapter takes the California budget story up through early August 2011. Later developments are not reflected in the text.

2 "Special Report: Democracy in California," *Economist*, April 23, 2011, special report section, p.5.

3 Quoted in David Siders, "Schwarzenegger leaves criticism of GOP Lawmakers behind, praises compromise on budget, *CapitolAlert* blog of *Sacramento Bee*, October 19, 2010.

4 Quoted in Jim Christie, "Brown budget plan too rosy for California investors," *Thomson Reuters*, October 21, 2010.

5 Quoted in Joe Garofoli, "If you hear a candidate say this magic phrase, they're in trouble," *Politics* blog of *San Francisco Chronicle*, October 29, 2010.

6 Judy Lin, "S&P: Calif's fiscal problems different from Greece," *InsideBayArea.com*, May 4, 2011. Greece had a much higher government debt to GDP ratio than California and had social insurance, social welfare, and military obligations far in excess of California's. The only similarity was that once Greece gave up its national currency for the euro, it became like California, borrowing in a currency it could not create or control.

7 Jack Chang, "Jerry Brown credited with election's best negative spot," *CapitolAlert* blog of *Sacramento Bee*, March 11, 2011. The columnist, Chris Cillizza, apparently consulted with other media reporters in making the selection.

8 The ostensible ground for legal action was that Whitman owed back pay to the housekeeper. A settlement of $5,500 was reached after the November election.

9 Quoted in Carla Marinucci, "Meg-bash! Whitman's post-election political autopsy at UC Berkeley brutally dissects 'worst campaign ever," *Politics* blog of *San Francisco Chronicle*, January 22, 2011.

10 "How California Voted: Exit Polling Nov. 2, 2010," *Sacramento Bee*, November 4, 2010. Whitman carried only voters 65 and older. The younger the voter, the higher the margin for Brown.

11 Governor Schwarzenegger characterized Whitman's position on exempting police pensions as "appalling." Seema Mehta and Michael J. Mishak, "Whitman, Brown exaggerate foe's stances on school funding and crime," *Los Angeles Times*, October 15, 2010. However, in various pension deals he struck with public unions as part of contract negotiations, he did not impose defined-contribution plans.

12 Don Novey quoted in Jon Ortiz, "Don Novey loses election gamble against Jerry Brown," *Sacramento Bee*, November 29, 2010. (Novey was a past president of another union, the California Correctional Peace Officers Association that had backed Brown. He became an advisor to the California Statewide Law Enforcement Association that followed is advice and backed Whitman.)

13 Allen Zaremberg quoted in Jack Chang, "State chamber head Zaremberg's relationship with Brown still up in the air," *Sacramento Bee*, December 30, 2010.

14 Quoted in John Myers, "A 'Comprehensive' Budget Deal Is...?," *KQED Capitol Notes*, March 3, 2011. The Chamber's general receptiveness to the Brown proposal angered conservatives. See Jon Fleischman, "The CalChamber Is Ready to Betray Taxpayers Again?," *Flashreport*, March 4, 2011.

15 Preliminary details and analysis on Whitman and Brown spending can be found in Lance Williams, "How Whitman spent $160 million," *California Watch blog*, November 2, 2010. About $144 million was estimated to be Whitman's own money. Jack Chang, "Meg Whitman postscript: another $2.6 million invested in campaign," *CapitolAlert*, November 17, 2010. A final report summary—which repeats the $144 million figure—can be found in Seema Mehta and Maeve Reston, "Jerry Brown nearly matched Meg Whitman's campaign spending on TV in final weeks of race," *Los Angeles Times*, February 1, 2011.

16 Carly Fiorina, another Silicon Valley business executive (from HP), was handily defeated in the general election for the U.S. Senate by incumbent Barbara Boxer. As in the Whitman case, Fiorina was forced in the three-way primary contest to take conservative positions that repelled voters in the general election. A notable example was endorsing in a TV debate the right of those persons on the "no-fly" list to have guns in an effort to compete with conservative Chuck DeVore. Moderate Tom Campbell, who did not think guns for those on the no-fly list was a good idea, noted that only in a Republican primary would anyone take the pro-gun position in that case.

17 Quoted in Seema Mehta, "Meg Whitman says the GOP must change its approach to immigration," *Los Angeles Times*, April 13, 2011.

18 Quoted in David Siders, "Jerry Brown tells state workers to take Republicans to lunch," *CapitolAlert* blog of *Sacramento Bee*, April 6, 2011

19 Quoted in Brian Joseph, "Tax system relies on wealthy," *HealthyCal*, April 7, 2011.

20 The data underlying the charts in this section are based on Tax Foundation figures. However, the Tax Foundation combines taxes paid by residents of states with taxes paid by those residents to other states. Taxes paid to other states are not relevant to cross-state comparisons. Moreover, the Tax Foundation makes assumptions about tax incidence of business taxes and assumes these are passed to consumers wherever in the U.S. the businesses sell. That assumption, however, means that individuals cannot "escape" such taxes by moving from one state to another. The assumption is particularly troublesome in the case of oil severance taxes. Oil prices are largely determined in world markets, a fact which suggests that the tax incidence of state severance taxes does not fall on retail consumers but rather on those firms extracting the oil. The data on the charts are based only on own-state taxes paid. Source of data: Tax Foundation, *State and Local Tax Burdens Fall in 2009 as Revenues Shrink Faster than Income*, Special Report no. 189, February 23, 2011.

21 Quoted in David Siders, "Brown Attributes win to skill, luck, and his 'sparkling personality,'" *CapitolAlert* blog of *Sacramento Bee*, November 3, 2010.

22 Quoted in David Siders, "Jerry Brown pledges bipartisan effort to resolve 'daunting' budget crisis," *Sacramento Bee*, Nov. 5, 2010.

23 Litigation blocked the sale-lease plan and after taking office, Governor Brown cancelled it, leading to further litigation by the developers that planned to buy the buildings.

24 Public Policy Institute of California, *December 2010: Californians & Their Government*, December 2010.

25 Public Policy Institute of California, *January 2011: Californians & Their Government*, January 2011.

26 Mike Genest, "Governor's reforms will help California," *Sacramento Bee*, December 21, 2010.

27 Anthony Adams was subjected to a recall. It did not succeed but he decided against running again. Mike Villines was deposed as Republican leader in the Assembly for going along with the tax increases. Villines ran in the 2010 GOP primary for insurance commissioner and almost lost to a completely unknown candidate whose main virtue to Republican voters was that he was not Villines. Villines was then defeated in the general election. Schwarzenegger also appointed a Senate ally on the budget, Roy Ashburn, to a state commission.

28 Litigation over the validity of the sentence reduction continued into summer 2011 and the controversy periodically bubbled up in the news media. The former governor made snoring sounds when asked about the issue by a TV reporter in April 2011, saying he was bored with questions on the subject, creating unfavorable publicity. Núñez had cooperated with Schwarzenegger in passing a universal health plan for California in the Assembly that later failed in the Senate. The plan was patterned after a program adopted in Massachusetts that eventually became a model for the Obama

federal plan. When pushed about whether his decision was in some respect a reflection of his relation with Núñez, Schwarzenegger said, "Well, Hello! I mean, of course, you help a friend." Quoted in Seema Mehta, "Schwarzenegger defends Núñez sentence reduction, slams Whitman," *PolitCal* blog of *Los Angeles Times*, April 18, 2011.

29 Michael Shields, "Schwarzenegger says governorship cost him $200 million," *Yahoo! News—Reuters*, January 14, 2011.

30 Quoted in Kevin Yamamura, "Lockyer regrets admitting he voted for Schwarzenegger in recall," *Sacramento Bee*, July 14, 2011.

31 Quoted in Jennifer Chaussee, "Anne Gus brings new dimension to the Horseshoe," *Capitol Weekly*, November 24, 2010.

32 Quoted in Ashley Powers and Anthony York, "Jerry Brown heads to Vegas to address prison guards union," *PolitiCal* blog of *Los Angeles Times*, December 6, 2010.

33 Quoted in Greg Lucas, "High court eyes Calif's landmark prison case," *Capitol Weekly*, May 12, 2012.

34 Governor Schwarzenegger also tried to put pressure on the legislature through state unions by trying to impose payment of state workers at the minimum wage when budgets were late. The argument was that absent a budget, there was no authorization to pay state workers other than at the minimum wage. (Workers would be made whole when the budget was passed.) However, his attempt to impose the minimum wage was thwarted by state controller John Chiang (whose office writes paychecks) who said antiquated state computers could not be reprogrammed to pay the minimum wage and meet required labor standards requirements. The issue was never settled—but no one was paid the minimum wage—during the Schwarzenegger governorship and Governor Brown inherited the litigation challenging Chiang's assertion. He dropped the lawsuit in February 2011 on the grounds that, indeed, the computers could not do the job without costly modifications.

35 Over 98% of the tax due went unpaid, according to a Board of Equalization estimate. See Jan Norman, "Report: 98.6% of tax for Internet sales not paid," *Orange County Register*, May 10, 2011.

36 Board of Equalization, *Revenue Estimate: Electronic Commerce and Mail Order Sales*, updated to December 6, 2010. Available at http://www.boe.ca.gov/legdiv/pdf/e-commerce-11-10.pdf

37 Since consumers owed the sales tax on out-of-state Internet purchases—even though they rarely paid it—the Amazon tax was technically not a tax measure. It was a tax *collection* measure referring to an existing tax and thus did not require a two-thirds legislative vote.

38 Brown said that "borrowing's not a free good" in a public forum in early December. That statement appeared to be a signal that he had changed his attitude toward borrowing that he had previously expressed. Quoted in John Myers, "Jerry, Meet Gridlock; Gridlock, Jerry," *KQED Capital Notes*, December 8, 2010.

39 The text of the inaugural address appears in "Third Inaugural Address," *Sacramento Bee*, January 3, 2011. The official text omits some impromptu remarks. When the governor introduced his 98-year old aunt, for example, he joked that opponents should take note of his genetic endowment of longevity.

40 Quoted in Shane Goldmacher, "State Treasurer warns IOUs could loom in April, May," *PolitiCal* blog of *Los Angeles Times*, January 22, 2011.

41 Quoted in Kevin Yamamura, "Brown to ask for deep cuts, five-year extension of taxes," *CapitolAlert* blog of *Sacramento Bee*, January 10, 2011.

42 Quoted in media release of January 10, 2011 issued by the Assembly Republican Caucus.

43 Quoted in Torey Van Oot, "GOP Leaders: No votes to put taxes on ballot," *CapitolAlert* blog of *Sacramento Bee*, January 10, 2011.

44 A special election would not have been confined to the tax extensions since any initiatives that had been certified as having sufficient signatures would also be on the ballot. (Certified initiatives go on the next statewide election, whenever that occurs.) There were two such initiatives, one relaxing term limits and the other imposing a $1/pack tax on cigarettes for cancer research.

45 Quoted in Shane Goldmacher, "Republicans won't offer own budget plan, lest they become 'the bad guys,'" *Los Angeles Times*, January 11, 2011.

46 Jann Taber, spokesperson for Senate Republican leader Bob Dutton, quoted in Kevin Yamamura, "Brown Countdown, Day 47: Democrats don't need GOP for tax vote, state's lawyers say," *Sacramento Bee*, February 26, 2011.

47 Quoted in Jim Sanders, "Pérez: 'No' to sidestepping GOP in tax extension vote," *Capital Alert* blog of *Sacramento Bee*, March 2, 2011.

48 *Howard Jarvis Taxpayers et al., v Debra Bowen, as Secretary of State, etc., Geoff Brandt, as State Printer, etc., Court of Appeal, Third Appellate District No. C060441, January 27, 2011.*

49 The next scheduled election—absent a special election in 2011—would have been the presidential primary set for February 2012. However, the legislature moved the primary to June 2012 to coincide with the state primary. So the legislative constitutional amendment (ACA 4) and—at this writing—two initiatives will be on the June 2012 primary ballot. One initiative proposes a tobacco tax earmarked for cancer research. The other proposes a relaxation of legislative term limits.

50 Legislative Analyst's Office, *The 2011-12 Budget: The Administration's Revenue Accrual Approach*, January 31, 2011.

51 On Table 5, the difference—in $ millions—between Brown's no-policy-change revenues for 2010-11 and his proposal for that year is $3,507 ($94,194-$90,687). For the next year, the difference is $6,183 ($89,696-$83,513). The revenue hike, combining the two is $9,690 for two years (about ($9.7 billion). The expenditure reduction for the two years is $584 in the first year plus $16,135 in the second for a total of $16,769 ($16.8 billion).

52 Quoted in John Myers, "Brown Dishes Jokes, Truth, to Locals," *KQED Capitol Notes*, January 19, 2011.

53 Quoted in Susan Ferriss, "Brown Countdown, Day 19: Home health care cuts face legal questions," *Sacramento Bee*, January 28, 2011.

54 Letter and attachment from State Auditor Elaine M. Howle to Governor Brown dated March 9, 2011.

55 Such agencies were authorized by the legislature in 1945 and permitted by voters to use property tax revenues in 1952. About 12% of property tax revenues go to redevelopment. There are complicated flows of such diverted property tax revenues by the agencies to locals—including school districts. But the state picks up the tab for about $2 billion per year diverted from K-14. Legislative Analyst's Office, *Governor's Redevelopment Proposal*, February 7, 2011.

56 Redevelopment agencies also have other sources of funds. About 83% of their revenues in fiscal year 2008-09 came from tax increment financing. Source: California State Controller, *Community Redevelopment Agencies Annual Report*, December 31, 2010.

57 A much smaller source of conflict with local governments involved the issue of mandates. Prop 4 (1979) and Prop 1A (2004) require the state to reimburse local governments of programs mandated on the locals by the state. However, if the legislature simply doesn't fund the mandate, locals are left with the choice of not operating the program or paying for it themselves. The proposed budget effectively suspended certain mandates that locals might have difficulty discontinuing, such as providing mail ballots to voters who request such ballots on a permanent basis.

58 A spokesperson for the Department of Finance stated that the proposal could "withstand any legal challenge." H.D. Palmer quoted in Kevin Yamamura, "Legislative counsel says Brown's redevelopment plan illegal," *CapitolAlert* blog of *Sacramento Bee*, May 3, 2011.

59 A Wall Street Journal/NBC poll at the time indicated that Americans generally disapproved of taking away collective bargaining rights for public workers but did favor worker concessions to help government budgets. See "WSJ/NBC Poll: Strong Support for Bargaining Rights," *Wall Street Journal* online, March 2, 2011.

60 Local governments, e.g., Orange County, California in the 1990s, the City of Vallejo, California in the 2000s, can declare bankruptcy under the existing legal framework.

61 The issue in Costa Mesa was a plan by the city council to privatize services and layoff a large fraction of city workers, as well as pensions. Litigation concerning the layoffs was still in progress at this writing.

62 The term "401k" refers to a section of the Internal Revenue Code. That section covers only private employees although there are other section numbers such as 403b and 457b that cover the public sector. However, the reference in the debates about public pensions commonly referred to 401k since that is what most people—who work in the private sector—understand.

63 Orange County in particular tried to undo a pension increase it had given to sheriff's deputies. A court ruling noted that even if the pension increase the County was trying to undo was imprudent, "imprudence... is not unconstitutional." Quoted in Kimberly Edds, "County takes deputies' pension fight to state Supreme Court," *Taxdollars* blog of *Orange County Register*, February 8, 2011.

64 See Liam Dillon, "The 401(k)'s Sticker Shock," *Voice of San Diego*, June 5, 2011, on the attempt by the City of San Diego to move to defined contribution and the discussion in that City of these points.

65 Quoted in Steve Harmon, "GOP senator: No pension reform, no vote on taxes," *Contra Costa Times*, January 24, 2011.

66 John Ehnes, executive director of CalSTRS, quoted in Timm Herdt, "State pension chiefs say cutting worker benefits would be illegal," *Ventura County Star*, March 2, 2011. See Little Hoover Commission, *Public Pensions for Retirement Security*, February 2011.

67 See Jeffrey Keefe, *Debunking the Myth of the Overcompensated Public Employee*, Economic Policy Institute Briefing Paper No. 276, September 15, 2010 (on public employment generally in the U.S.), http://www.employmentpolicy.org/sites/www.employmentpolicy.org/files/Debunking%20the%20Myth.pdf; Sylvia A. Allegretto and Jeffrey Keefe, *The Truth About Public Employees in California*, Policy Brief, Institute for Research on Labor and Employment, University of California-Berkeley, October 2010, http://www.irle.berkeley.edu/cwed/wp/2010-03.pdf; California Foundation for Fiscal Responsibility, *Comparing Public and Private Employee Compensation and Retirement Benefits in California*, Capitol Matrix Study, May 2011, http://www.fixpensionsfirst.com/comparing-public-and-private-employee-compensation-and-retirement-benefits-in-california/ ; CalPERS, "Pension Reform Proposals Raise Serious Concerns; Study Comparing Private and Public Benefits is Flawed," media release, May 12, 2011.

68 There are two legacy organizations that descend from the Prop 13 (property tax limitation) campaign of 1978. One—Peoples Advocate—filed an elaborate pension initiative in July 2011 and appeared to be fishing for a financial angel to fund a campaign. (Peoples Advocate kicked off the 2003 recall drive against Governor Gray Davis—but the funding for that drive came from other sources.) The other Prop 13 legacy organization—the Howard Jarvis Taxpayers Association—indicated it was not interested in taking on the pension issue in 2012.

69 Both quotes from Steve Yeater, "New Governor, Familiar Fight?," *KQED Capitol Notes*, January 31, 2001.

70 California State Controller, "*Statement of General Fund Cash Receipts and Disbursements, January 2011*," p. A2.

71 Legislative Analyst's Office, letter to State Senator Mark Leno with exhibits, February 10, 2011.

72 Quoted in Susan Ferriss, "Brown's Countdown, Day 39: Dutton says Senate GOP won't vote to place taxes on ballot," *Sacramento Bee*, February 17, 2011.

73 Quoted in John Howard, "Surprises loom as election debate picks up steam," *Capitol Weekly*, February 17, 2011.

74 Quoted in John Myers, "Question Time With Jerry Brown," *KQED Capitol Notes*, February 24, 2011.

75 Chancellor Robert Birgeneau quoted in John Loo, "Chancellor: UC Berkeley morphing into federal university," *CaliforniaWatch*, February 23, 2011.

76 Quoted in Jack Chang, "Jerry Brown says he's meeting with Republicans on taxes," *CapitolAlert* blog of *Sacramento Bee*, March 4, 2010.

77 John Coupal, president of the Howard Jarvis Taxpayers Association, weekly online newsletter, March 8, 2011.

78 The letter was made available on the web at http://www.scribd.com/doc/50227118/110307-letter

79 Wyatt Buchanan and Marisa Lagos, "GOP faction presses party's legislators on budget," *San Francisco Chronicle*, March 15, 2011.

80 Quoted in Kevin Yamamura, "Brown's Countdown, Day 70: An all-cuts budget may surface," *Sacramento Bee*, March 20, 2011.

81 Quoted in Wyatt Buchanan, "Gov. Brown: Tax vote will happen 'one way or another,'" *Politics* blog of *San Francisco Chronicle*, March 21, 2011.

82 Quoted in John Myers, "In Search of Budget Dénouement," *KQED Capital Notes*, March 23, 2011.

83 John Howard, "Tensions in organized labor over Brown's redevelopment plan," *Capitol Weekly*, March 21. 2011.

84 Jim Miller, "RDA's issue hundreds of millions in bonds," *PE Politics* blog of *Riverside Press-Enterprise*, March 21, 2011.

85 As it happened, A. Alan Post, the legendary Legislative Analyst who successfully opposed the Reagan spending cap plan in the 1970s, died at around the time the new cap initiative was filed.

86 California Field Poll, "More California Voters Now View Public Pension Benefits as Too Generous," March 17, 2011. Note the misleading title of the release. In fact, as the text discusses, more voters thought the benefits were about right or not generous enough. The "more" in the title refers to the fact that relative to October 2009, the proportion saying "too generous" had risen.

87 George Skelton, "There's blame to go around," *Los Angeles Times*, March 31, 2011.

88 Quoted in "Jerry Brown: Hug a Republican," *CapitolAlert* blog of *Sacramento Bee*, April 6, 2011.

89 California Field Poll, "Voters Approve of Governor Brown's Job Performance by Greater Than Two to One Margin," March 22, 2011.

90 Quoted in "Bob Dutton: Jerry Brown's wife 'yelled' at him," *CapitolAlert*, March 31, 2011.

91 Quoted in David Siders, "Jerry Brown defends first lady in LA interview," *CapitolAlert* blog of *Sacramento Bee*, April 10, 2011.

92 Barbara Anderson, "Valley First 5s to sue state over fund grab," *Fresno Bee*, April 5, 2011.

93 The Sacramento First Five commission cut back programs in early May.

94 UC-San Diego chancellor Marye Anne Fox quoted in Pauline Repard, "UCSD, Cal Western talks for law school suspended," *San Diego Union-Tribune*, April 6, 2011.

95 Gene Block, "Cuts to higher education: The Master Plan turncoats," *Los Angeles Times*, April 17, 2011. Note that titles to op eds are not always composed by the authors. The newspaper's editors may create the titles. It is unclear whether Block intended to label the Republicans as "turncoats" since no such language appears in the text of the op ed.

96 Kevin Yamamura, "Brown's Countdown: Day 94: Teachers seek tax hike without an election," *Sacramento Bee*, April 13, 2011.

97 David Siders, "Jerry Brown mulling tax extension before public vote," *CapitolAlert* blog of *Sacramento Bee*, April 8, 2011.

98 Quoted in Josh Richman, "Lockyer: Let further cuts start in GOP districts," *Political Blotter* blog of *Contra Costa Times*, April 26, 2011.

99 Torey Van Oot, "Steinberg considers cuts targeting GOP districts," *CapitolAlert* blog of *Sacramento Bee*, April 27, 2011.

100 Gil Duran quoted in Jim Miller, "Efforts to restore new cities' funding under way in Capitol," *Riverside Press-Enterprise*, July 7, 2011.

101 Various other numbers were used in the debate over the above-estimate receipts. The figures in the text come from California State Controller, "Statement of General Fund Cash Receipts and Disbursements: April 2011," May 2011.

102 Quoted in John Myers, "Teachers: More Money for Schools. GOP: Okay," *KQED Capital Notes*, May 9, 2011.

103 Quoted in Torey Van Oot, "Brown, Steinberg differ on how soon election should come," *Capital Alert* blog of *Sacramento Bee*, May 16, 2011.

104 Dutton and Pérez quoted in Torey Van Oot, "Rapid Response Roundup: Brown's May budget revision," *CapitolAlert* blog of *Sacramento Bee*, May 16, 2011.

105 Public Policy Institute of California, *Californians & Their Government: May 2011*, June 1, 2011.

106 California Field Poll, "Voters Don't Have Great Confidence in Governor or Legislature to Resolve Budget Deficit," June 15, 2011. In the Field Poll, 49% favored an election; 45% opposed it, and the remainder didn't know.

107 Quoted in David Siders, "At prayer breakfast, Jerry Brown asks to consider 'lost souls,'" *Sacramento Bee*, May 19, 2011.

108 When the pay-forfeit provision was enforced by state controller John Chiang after June 15 (see below in the text), he interpreted Prop 25 to require a budget that was "balanced" by citing a provision passed by voters in 2004 as part of Governor Schwarzenegger's budget financing propositions of that period. See David Siders, "Chiang to withhold lawmaker pay if budget deadline passes," *Capital Alert* blog of *Sacramento Bee*, June 2, 2011.

109 Quoted in David Siders, "Chiang to withhold lawmaker pay if budget deadline passes," *CapitolAlert* blog of *Sacramento Bee*, June 2, 2011.

110 Quoted in Kevin Yamamura, "John Chiang's pay blockage upends budget talks," *Sacramento Bee*, June 22, 2011.

111 Quoted in Dave Paresh, "Niello's pension reform initiative enters signature-gathering phase," *State Worker* blog of *Sacramento Bee*, May 24, 2011 (updated version).

112 Quoted in David Siders, "Jerry Brown readies 'blue pencil' to keep spending cuts intact," *Capital Alert* blog of *Sacramento Bee*, June 2, 2011.

113 Quoted in Anthony York, "Jerry Brown says budget talks hit a new snag," *PolitiCal* blog of *Los Angeles Times*, June 7, 2011.

114 SEIU California State Council executive director David Kieffer quoted in Kevin Yamamura, "Union chief says Jerry Brown's tax vote is 'fraught with peril,'" *Sacramento Bee*, June 9, 2011.

115 Senator Bob Huff quoted in Torey Van Oot, "Senate OKs local tax authority bill after 'tax bridge' falls short," *CapitolAlert* blog of *Sacramento Bee*, June 10, 2011.

116 Christina Jewett, "Nursing homes reach last-minute deal on Medi-Cal cut," *California Watch*, June 22, 2011.

117 Quoted in Shane Goldmacher and Anthony York, "California Democrats pass budget with taxes, cuts and tricks," *Los Angeles Times*, June 16, 2011.

118 Quoted in John Myers, "Brown's Budget 'Fuzzy Zone," *KQED Capital Notes*, June 13, 2011.

119 Quotes from David Siders, "Jerry Brown says he'll 'move heaven and earth' for budget deal," *CapitolAlert* blog of *Sacramento Bee*, June 16, 2011 and official governor's message of June 16, 2011.

120 On June 18, two days after the veto, Brown said at a public gathering that "I may be in initiative circulation... in the next few months." Quoted in Anthony York, "Jerry Brown warns GOP legislators he may go around them," *Los Angeles Times*, June 18, 2011.

121 Kevin Yamamura, "Chamber CEO says still time for 'comprehensive' deal," *CapitolAlert* blog of *Sacramento Bee*, June 20, 2011.

122 Quoted in Torey Van Oot, "Steinberg to halt confirmation of Brown's appointees," *CapitolAlert* blog of *Sacramento Bee*, June 17, 2011.

123 Quoted in David Siders, "Jerry Brown calls Steinberg action 'small price to pay,'" *CapitolAlert* blog of *Sacramento Bee*, June 17, 2011.

124 Quoted in Kevin Yamamura, "Steinberg raises legal questions about withholding pay," *CapitolAlert* blog of *Sacramento Bee*, June 20, 2011.

125 Republican senator Bob Huff quoted in Kevin Yamamura, "Senate GOP budget vice chair opposes pay blockage," *CapitolAlert* blog of *Sacramento Bee*, June 21, 2011.

126 Quoted in Kevin Yamamura, "Treasurer Bill Lockyer believes Dems' budget not financeable," *CapitolAlert* blog of *Sacramento Bee*, June 16, 2011.

127 Howard Jarvis Taxpayers Association, media release of June 21, 2011.

128 Quoted in Shane Goldmacher and Evan Halper, "California Controller John Chiang's unlikely turn in the spotlight," *Los Angeles Times*, June 23, 2011. See also George Skelton, "Bad Policy, but it may work," *Los Angeles Times*, June 23, 2011.

129 Statement released by Darrell Steinberg, June 27, 2011.

130 Quoted in Kevin Yamamura, "Budget deal by Brown, Dems scraps tax election, may trigger cuts," *Sacramento Bee*, June 28, 2011.

131 The governor used his line-item veto to reduce General Fund expenditures by $23.8 million. Much of his vetoing fell outside the General Fund.

132 However, the legislature instructed school districts effectively to ignore the possibility of the trigger firing, assume

the same level of funding as the prior year, and to avoid layoffs in planning their 2011-12 budgets. Not surprisingly, school district administrators protested. The superintendent of the large LA Unified School District said the constraint would have "detrimental effects on all students." John Deasy quoted in Connie Llanos, "LAUSD's Deasy wants funding measures repealed," *Los Angeles Daily News*, July 29, 2011.

133 Quoted in Jim Sanders, "Lockyer gives thumbs up to Democrats' budget deal," *CapitolAlert* blog of *Sacramento Bee*, June 28, 2011.

134 Quoted in Anthony York, "Jerry Brown laments 'atrophying' political process," *PolitiCal* blog of *Los Angeles Times*, August 2, 2011.

135 Brown had said in early April 2011 that tuition at UC could rise to at least $20,000. See "Brown warns of more UC tuition hikes," *KGO* website, April 6, 2011.

136 In effect, redevelopment agencies could continue if they paid a price to the state. Some agencies did agree rather than be terminated. There was also the possibility of a referendum challenging the car fee but no such filing had been made as of this writing.

137 The bill would have forbidden piece-rate type payments (payments per signature) and required that signature gatherers be paid by the hour. Since such gatherers are hard to monitor, the bill would have created what economists call an "agency problem," making the process more costly.

138 The radio ad was apparently aimed at an initiative being circulated—a so-called "paycheck protection" law—that would make it more difficult for unions to use dues money for political purposes. Voters have rejected such initiatives in elections in 1998 and 2005.

139 The legislative counsel affirmed this interpretation in the case of the "Amazon tax," the budget element that required out-of-state online retailers to collect and remit California sales tax. There would be a period from July 1 to the date the referendum petition was certified as having sufficient signatures in which the tax would be in effect. It would then be suspended until the election. See letter of the Legislative Counsel Bureau of Senator Joel Anderson of July 22, 2011. Amazon was—in any case—refusing to comply so that once its payments were due, there would presumably be litigation on whether the money was owed.

140 The case—*Brown vs. Rincon Bank of Luiseno Mission Indians*—had challenged a revenue sharing deal Governor Schwarzenegger had tried to impose on a particular tribe. The decision, favoring the tribe, potentially undermined other deals with tribes. See John Myers, "State Poised to Lose Indian Casino Cash?," *KQED Capital Notes*, July 8, 2011.

141 As part of realignment, various state functions and corresponding revenues were shifted to local governments. That step—by reducing the state budget—was viewed by those writing the budget as reducing the state's funding requirements for K-14 under Prop 98. Normally, a legal challenge of that type might be brought by teacher unions. But—as noted in the text—unions had received teacher layoff protections as part of the budget deal and so did not challenge the outcome.

142 Even before the 2011-12 budget was enacted, courts were ordering the state to spend more on various programs. See, for example, Bob Egelko, "Judge orders California to boost foster payments," *San Francisco Chronicle*, June 1, 2011.

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